Supreme Court, U.S.
FILED
07-484 OCT 9 - 2007
OFFICE OF THE CLERK

69

No. 07-(1)

IN THE

Supreme Court of the United States

SEMEN LEYKIN, *et al.*,

Petitioners,

v.

AT&T CORPORATION, *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

CHRISTOPHER LOVELL
Counsel of Record
GARY S. JACOBSON
IAN T. STOLL
LOVELL STEWART HALEBIAN LLP
500 Fifth Avenue
New York, New York 10110
(212) 608-1900

Counsel for Petitioners

211386

COUNSEL PRESS
(800) 274-3321 • (800) 359-6859

QUESTIONS PRESENTED

The control person of the issuer of stock used lies to the market for that stock to misappropriate the issuer's intellectual property ("IP") and customers. Initially, the control person's deceptions increased the price of that stock while the control person successfully misappropriated certain parts of the issuer's IP. Later, the control person's lies somewhat decreased the stock price in order to gain increased control over the issuer and pressure the management of the issuer into complying with the control person's demands for the most sensitive portions of the issuer's IP. After completing its misappropriation of the IP, the control person consummated its scheme by forcing the issuer into bankruptcy and taking its customers. Plaintiffs purchased the issuer's stock at the increased market prices and sold the stock at the somewhat decreased market prices caused by the control person's scheme.

The questions presented are:

1. Whether an integrated scheme of misrepresentations and the unlawful acts they conceal qualify as a scheme or artifice in connection with the purchase or sale of the security within the meaning of Securities and Exchange Commission ("SEC") Rule 10b-5, 17 C.F.R. § 240.10b-5, or, as the Court below held, a scheme in connection with the purchase or sale of the security is limited to misrepresentations and excludes the associated deceptive or unlawful acts they are designed to conceal?

2. Whether pleading loss causation in a Rule 10b-5 scheme claim requires merely allegations that the "act . . . of the defendant alleged to violate this chapter caused the loss" as set forth in 15 U.S.C. § 78u-4(b)(4) or, as the Court below held, plaintiff must invariably plead that loss was caused by either a disclosure to the market of the misrepresentation or a materialization of the risk concealed by the misrepresentation?

RULES 14.1 AND 29.6 STATEMENT

Petitioners (plaintiffs-appellants below) are Semen Leykin, Frank Thomas, Ken Pearlman, Mike Katto, At Home Suit Group, Inc., Kurt Buettler, Gerry Galiger, Stan Cohn, Channa Unger, Michael Eksler, Frieda Eksler and Ronald Ventura.

At Home Suit Group, Inc. has no parent corporations and no publicly held companies own 10% or more of its common stock.

Respondents (defendants-appellees below) are AT&T Corporation, C. Michael Armstrong, Mark McEachen, Frank Ianna, Charles H. Noski, Daniel H. Somers, Hossein Eslambolchi, Raymond Liguori, and Mohan Gyani.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
RULES 14.1 AND 29.6 STATEMENT	iii
TABLE OF CONTENTS	iv
TABLE OF APPENDICES	viii
TABLE OF CITED AUTHORITIES	ix
OPINIONS BELOW	1
JURISDICTION	1
STATUTES AND REGULATIONS INVOLVED	1
STATEMENT OF THE CASE	2
1. The AT&T Defendants' Scheme To Lie To The Market For At Home Stock In Order To Misappropriate At Home's Proprietary Technology And Customers	2
2. At Home's "Critical" Proprietary Technology Entitled At Home To 30% Of AT&T's Revenues From At Home's Service	2

Contents

Page

3. The AT&T Defendants' Nineteen Misappropriations And $400,000,000 Payment To The Bankrupt At Home Bondholders' For Misappropriating At Home's Intellectual Property 5

4. Chronology: The AT&T Defendants Had To Make Escalating Misrepresentations In Order To Enable Them To Misappropriate At Home's Most Sensitive Intellectual Property 6

   a. The Initial Misrepresentations Inflated The Price of At Home Stock 6

   b. Some of The Scheme's Later Misrepresentations Decreased At Home's Stock Price Substantially .. 8

   c. False Representations To Agree To Buy Control Blocks of Stock At The Reduced Price 10

   d. AT&T's Continued Deceptive Statements Consummate Its Scheme 13

5. Procedural History 14

Contents

Page

REASONS FOR GRANTING THE PETITION 15

I. IN CONFLICT WITH OTHER CIRCUITS, THIS COURT'S OWN PRIOR DECISIONS, AND THE PLAIN LANGUAGE OF RULE 10b-5, THE ORDER EFFECTIVELY LIMITS THE SCOPE OF CONDUCT PROHIBITED BY RULE 10b-5 SOLELY TO MISREPRESENTATIONS 18

A. Conflicts With Prior Decisions Of This Court 18

B. The Order Conflicts With The Plain Language Of The Statute And Rule 25

C. Conflict With Other Circuits 28

II. THE ORDER'S LOSS CAUSATION RULING CONFLICTS WITH 15 U.S.C. § 78u-4(b)(4) AND THE PRIOR DECISIONS OF THIS COURT 31

A. Conflict with 15 U.S.C. § 78u-4(b)(4) 31

Contents

Page

B. Conflict With The Prior Decisions Of This Court 33

III. OTHER REASONS FOR GRANTING THE PETITION 34

CONCLUSION 35

TABLE OF APPENDICES

Page

Appendix A — Summary Order Of The United States Court Of Appeals For The Second Circuit Filed January 30, 2007 ..... 1a

Appendix B — Opinion And Order Of The United States District Court For The Southern District Of New York Dated March 23, 2006, As Amended June 26, 2006 ..... 6a

Appendix C — Memorandum Endorsement 46a

Appendix D — Memorandum Endorsement ... 51a

Appendix E — Order Of The United States Court Of Appeals For The Second Circuit Denying Petition For Rehearing Filed July 9, 2007 ... 54a

Appendix F — Statutes And Regulations Involved 56a

TABLE OF CITED AUTHORITIES

Page

Federal Cases

Affiliated Ute Citizens v. United States, 406 U.S. 128 (1972) 16, 18, 25, 28

Basic, Inc. v. Levinson, 485 U.S. 224 (1988) ... *passim*

Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975) 27

Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A., 508 U.S. 959 (1993) ... 26

Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A., 511 U.S. 164 (1994) ... 26

Duncan v. Walker, 533 U.S. 167 (2001) 27

Dura Pharmaceuticals v. Broudo, 544 U.S. 336 (2005) ..... *passim*

Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976) 27, 32

Herman & MacLean v. Huddleston, 459 U.S. 375 (1983) 28

Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit, 547 U.S. 71 (2006) 22

Cited Authorities

Page

Mutual Shares Corp. v. Genesco, Inc., 384 F.2d 540 (2d Cir. 1967) ..... *passim*

Pinter v. Dahl, 486 U.S. 622 (1988) 28, 34

Regents of the University of California v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 482 F.3d 372 (5th Cir. 2007) 15, 30, 31

Santa Fe Indus. v. Green, 430 U.S. 462 (1977) 19, 26, 27, 28

SEC v. Capital Gains Research Bureau, 375 U.S. 180 (1963) 18, 19, 25, 28

SEC v. Zandford, 535 U.S. 813 (2002) ..... *passim*

Simpson v. AOL Time Warner, Inc., 452 F.3d 1040 (9th Cir. 2006) 15, 28, 29

Stoneridge Investment Partners v. Scientific-Atlanta, Inc., 127 S.Ct. 1873 (2007) ..... *passim*

Superintendent of Ins. of N.Y. v. Bankers Life & Casualty Co., 404 U.S. 6 (1971) ..... *passim*

Superintendent of Ins. of N.Y. v. Bankers Life & Casualty Co., 430 F.2d 355 (2d Cir. 1970) 22

United States v. Nordic Village, Inc., 503 U.S. 30 (1992) 27

Cited Authorities

Page

Federal Statutes

15 U.S.C. § 78j(b) 1

15 U.S.C. § 78u-4(b)(4) ..... *passim*

28 U.S.C. § 1254(1) 1

Federal Regulations

17 C.F.R. § 229.404(a) 1, 12, 21

17 C.F.R. § 240.10b-5 ..... *passim*

Other Authorities

Miller, M. & Modigliani, F., *Dividend Policy, Growth, and the Valuation of Shares*, 34 J.Bus. 411 (1961) 4

Petitioners, purchasers of the publicly-traded stock of Excite At Home Corp., respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit.

OPINIONS BELOW

The opinion of the court of appeals (Petition Appendix ("App.") 1a-5a) is reported at 216 Fed. Appx. 14. The opinion of the district court (App. 6a-45a) is reported at 423 F.Supp.2d 229.

JURISDICTION

The judgment of the court of appeals was entered on January 30, 2007. Petitioners filed a timely petition for rehearing and rehearing en banc on February 14, 2007, which was denied by order dated July 9, 2007. App. 54a-55a. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS INVOLVED

The relevant statutory and regulatory provisions, Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (the "Exchange Act"), Section 21D(b)(4) of the Exchange Act, 15 U.S.C. § 78u-4(b)(4), SEC Rule 10b-5, 17 C.F.R. § 240.10b-5, and SEC Regulation S-K, Item 404(a), 17 C.F.R. § 229.404(a), are reproduced at App. 56a-58a.

STATEMENT OF THE CASE

1. The AT&T Defendants' Scheme To Lie To The Market For At Home Stock In Order To Misappropriate At Home's Proprietary Technology And Customers

Plaintiffs, including lead plaintiffs Frank Thomas and Ken Pearlman, bought Excite At Home ("At Home") common stock between November 8, 1999 and September 29, 2001 ("Class Period") at the prices prevailing on the efficient NASDAQ market for At Home stock. ¶¶13-14,Ex.A;JA2081,2154.

The prices at which they purchased and sold the stock were based on defendants' public statements and other publicly available information. *Basic, Inc. v. Levinson*, 485 U.S. 224, 246-247 (1988).

2. At Home's "Critical" Proprietary Technology Entitled At Home To 30% Of AT&T's Revenues From At Home's Service

Through its patented and other intellectual properties, At Home enjoyed a dominant position in bringing high-speed Internet access to homes and businesses over existing cable television lines. ¶¶2,55;JA2078,2091-92.

So superior were At Home's proprietary technologies that large cable television companies were At Home's principal customers, owned a majority of its voting stock,

and held a majority of the seats on its Board of Directors.[1]

AT&T Corporation ("AT&T") was the largest shareholder of At Home. ¶39(r);JA2104.

As a company with publicly traded stock, At Home made regular filings with the Securities and Exchange Commission ("SEC"). These filings were signed by directors of At Home, including those AT&T defendants who were At Home directors. ¶¶20-35;JA2082-86. Also,

---

1. The AT&T defendants are AT&T Corporation ("AT&T"), C. Michael Armstrong, Frank Ianna, Mohan Gyani, Charles H. Noski, Daniel H. Somers, John C. Petrillo, Raymond Liguori and Hossein Eslambolchi. ¶¶16,21,23,27,31,36; JA2081-86. All the AT&T defendants except for AT&T and Eslambolchi served as directors of At Home. ¶36;JA2086. The other defendants are as follows.

Defendants Cox and AT&T were At Home's largest customer and largest shareholder. Comcast also was a major shareholder and large customer of At Home. Their respective designees, defendants David Woodrow and Brian Roberts, were Series B directors of At Home whose unanimity was required for certain board actions. ¶¶17-18,33,35;JA2082,2085,2086.

Edward S. Rogers was a Class A director for the public shareholders, a substantial shareholder, and his cable company was a substantial customer of At Home. ¶34;JA2085-86.

Defendant Dr. John C. Malone was a large shareholder and director of both AT&T and At Home. SPA11,¶32;JA208,1325.

Non-Customer Defendants. Defendant Kleiner Perkins Caufield & Byers owned an interest in At Home and appointed two directors, defendants L. John Doerr and William R. Hearst III, who also was a Class A director for the public shareholders. ¶¶19,28,29;JA2082;2084. Defendants George Bell and Thomas A. Jermoluk were CEOs and directors, and defendant Mark McEachen was Chief Financial Officer of At Home. ¶¶20,22,29;JA2082-84.

AT&T was responsible as a control person of At Home under Section 20(a) of the Securities Exchange Act of 1934. ¶16;JA2081-82. In At Home's filings with the SEC, the following representation was made repeatedly:

> We regard our intellectual property, including our patents, copyrights, trademarks, trade secrets, and similar intellectual property as critical to our success. We rely upon patents, trademark and copyright law, trade secret protection and confidentiality or license agreements to protect our proprietary rights.

¶¶59(x),65(a),96;JA2106,2110-11,2131.

The foregoing protection of At Home's proprietary and "critical" intellectual property enabled At Home to continue to charge its cable customers approximately 30% of the fees for the monthly subscriptions that the cable companies charged their customers. ¶¶91(e),98;JA2127-28,2131-32. This protection of At Home's proprietary intellectual property justified NASDAQ's market expectations of a substantial future cash flow for At Home, ¶8;JA2080, and a substantial At Home stock price. *Id.*[2]

Without this protection, At Home had virtually nothing, and its stock was worth virtually zero. ¶6;JA2079. However, by September 1999, the AT&T defendants had formulated an undisclosed scheme to lie to the market for At Home stock in order "to drain all of

---

2. Merton H. Miller & Franco Modigliani, *Dividend Policy, Growth, and the Valuation of Shares*, 34 J.Bus. 411 (1961).

the proprietary technology out of At Home" (¶98(f);JA2132), use At Home's technology to start a competing business at AT&T (¶¶6,59(e);JA2079,2095), "weaken At Home's financial situation" (¶91(d);JA2127), "end At Home's life" (¶93;JA2129), and "inherit At Home's customers." ¶¶80,86,89(b),98(f),100,103; JA2119,2124-25,2132,2134.[3]

3. The AT&T Defendants' Nineteen Misappropriations And $400,000,000 Payment To The Bankrupt At Home Bondholders' For Misappropriating At Home's Intellectual Property

Pursuant to this scheme, the AT&T defendants' misrepresentations enabled them to commit at least **nineteen** separate misappropriations of At Home's intellectual property. ¶¶59,65,77,79-92,100,103,107; JA2094,2210,2118-28,2132,2134,2135. Each of these takings is alleged in great detail in plaintiffs' complaint. *Id.*

---

3. Except for AT&T, At Home's customer shareholders were all cable television, not technology, companies. ¶¶3,49,52;JA2078, 2089-90. AT&T had vast experience in various "narrow band" technologies. But AT&T had no experience with the specific broad band technology that At Home had mastered in order to bring high-speed internet access to homes and offices over television cables.

Also, AT&T had gone deep into debt (80 billion dollars) on a "bet the company" scheme to become the largest cable television operator. ¶¶55(c),59(c); JA2092,2094. AT&T was going to make this bet pay off by transforming its cable wires into a high-speed internet. ¶¶59(e),59(i),59(q),63(a)-(b); JA2095,2097,2104,2109. But, in order to service this debt, AT&T wanted to keep the 30% of its revenues that it was paying to At Home and also obtain for itself At Home's revenues from cable customers Cox and Comcast (*see* fn.1) by misappropriating At Home's intellectual property. ¶¶3,59(c),66; JA2078,2094,2111-12.

AT&T's extremely high number of misappropriations just happened to encompass **all aspects of At Home's intellectual property.** ¶¶6,59-65;77-89;JA2079,2094-2111,2118-2126. This included At Home's patented network architecture (¶81;JA2120), At Home's proprietary technology for implementing that architecture (¶¶81-83;JA2120-22), At Home's proprietary technology for customer communications, and all other aspects of At Home's proprietary technology and know-how. ¶¶84-85;JA2122.[4]

As a result of the foregoing, AT&T paid $400,000,000 to settle the bankrupt At Home bondholders' claims that AT&T misappropriated At Home's proprietary technology in order to start a competing business and supplant At Home. ¶¶6,59(e) and (q),87;JA2079,2095, 2104,2124.

4. Chronology: The AT&T Defendants Had To Make Escalating Misrepresentations In Order To Enable Them To Misappropriate At Home's Most Sensitive Intellectual Property

a. The Initial Misrepresentations Inflated The Price of At Home Stock

During September-November 1999, AT&T was able to misappropriate At Home's important proprietary back office system ("BOS") technology for data searches and

---

4. AT&T also acquired expensive hardware that copied the proprietary hardware that At Home used to operate its proprietary technology and network. ¶¶88,110-111;JA2124,2136. AT&T, per Scott Russell and others, admitted to At Home engineers that AT&T intended to use At Home's proprietary technology, which AT&T had taken on AT&T's duplicate "head end" hardware in order to duplicate At Home's service. ¶¶79(c);JA2119,2124.

troubleshooting; without this, AT&T could never have started its competing network. ¶¶58(g)-(h) and (j),118;JA2096-97,2140.

In order to avoid detection of their misappropriation of At Home's intellectual property and continue their scheme without detection, the AT&T defendants had to participate in lies contained in At Home's representations to the market for At Home stock. For example, in At Home's filings with the SEC on and before November 16, 1999, it was represented as follows:

> We regard our intellectual property, including our patents, copyrights, trademarks, trade secrets, and similar intellectual property as critical to our success. We rely upon patents, trademark and copyright law, trade secret protection and confidentiality or license agreements to protect our proprietary rights.

¶¶59(x),65(a),96;JA2106,2110-11,2131. This representation was false and misleading for many reasons. These included the AT&T defendants' undisclosed scheme and misappropriations, and the fact that the represented confidentiality and trade secret protections were not in place between At Home and, its largest customer, AT&T. ¶¶59(x),65(b);JA2106,2111,2131.

Absent disclosure of these misappropriations and the malign scheme of At Home's largest customer and shareholder to destroy At Home, persons purchasing At Home's stock on the efficient NASDAQ market bought into twin mirages: (1) a "normal company mirage" in which the largest customer and shareholder of At Home

was apparently not out to destroy At Home; and (2) a "proprietary technology mirage" in which At Home's apparently exclusive control and possession of its proprietary "keys to the internet" technology provided reasonable expectations of substantial future cash flow.

The AT&T defendants' undisclosed scheme artificially inflated the prices of At Home stock throughout the Class Period.

b. Some of The Scheme's Later Misrepresentations Decreased At Home's Stock Price Substantially

However, resistance by At Home officers stopped AT&T from misappropriating many other parts of At Home's proprietary intellectual property **during 1999.** ¶¶59(k),118(A)(1);JA2097-2102,2141. Without At Home's more important intellectual property, AT&T could not duplicate At Home's proprietary technology, end its payments to At Home, and take At Home's customers.

In order to overcome such resistance, the AT&T defendants escalated their scheme and began themselves to make direct misrepresentations to the market for At Home stock. AT&T intended these misrepresentations to reduce At Home's stock price, weaken At Home into complying with AT&T's demands for At Home's most important intellectual property and increase AT&T's control over At Home. *E.g.*, ¶¶49(k),60,91(b)-(d),100,103,119;JA2097,2107,2126-27,2132,2134,2147. These deceptions did reduce At Home's stock price and somewhat reduce the artificial inflation of such price caused by the undisclosed scheme.

On December 6, 1999, over At Home's objections, and at a time when At Home was preparing for a new equity issuance, AT&T represented that AT&T supposedly would implement customer choice for internet companies other than At Home (*i.e.*, "open access"). ¶¶59(k),118(A)(1);JA2097,2141. This "open access" representation was false because AT&T never intended to implement and never did implement open access. ¶60;JA2107. On the contrary, AT&T's corporate properties and interests were harmed in many ways by open access and AT&T actively opposed open access in legal briefs. *Id.* However, simultaneously with this "sham" public announcement, AT&T made internal demands upon At Home to turn over virtually all of its proprietary technology to AT&T based on the pretext of a need to prepare to conduct tests for "open access". ¶79(a);JA2097-98. Although open access was never implemented and AT&T never intended to implement it, the weakened At Home did turn over further intellectual property to AT&T in connection with the open access tests. ¶¶59(f) and (k);JA2095-2102.

AT&T's false December 6, 1999 announcement made pursuant to the scheme caused the price of At Home stock to plummet by 15% (and by more thereafter). ¶59(k);JA2097. This partially decreased the inflation that AT&T's scheme had earlier caused.

c. False Representations To Agree To Buy Control Blocks of Stock At The Reduced Price

Still, At Home's officers sought to refuse to divulge to AT&T the most sensitive intellectual property that AT&T needed to duplicate At Home's technology. This caused AT&T to commit its second, escalating misrepresentation in late March 2000. AT&T then announced that, subject to At Home's stockholders' approval, AT&T had agreed to purchase the control blocks of At Home stock held by defendants Cox and Comcast (*see* fn. 1) by paying more than $1,000,000,000 in AT&T stock to each. Such purchase price was to be at the then market price of At Home stock. This price had been decreased by AT&T's "open access" representation, thereby providing AT&T with a substantially lower cost to purchase the Cox and Comcast control blocks of At Home's stock. ¶63;JA2109. AT&T's purchase was subject to approval by At Home shareholders and, if approved, would increase AT&T's position to 23% equity control, and 74% overall voting control, of At Home. ¶70(b);JA2114.

In order to secure shareholder approval of these purchase transactions,[5] AT&T, per defendant Armstrong, its Chairman, represented in a stock market "squawk box" public interview that the March 28, 2000 Agreements were a "new commitment by AT&T . . . to

5. At Home's Class A shares were owned by the public shareholders. AT&T had no voting control over those shares. The separate approval of the Class was necessary to approve the transactions necessary for AT&T's purchases of the At Home stock owned by Cox and Comcast.

. . . [At Home]", which should "eliminate the uncertainty" about At Home. ¶63(a);JA2109. Defendant Armstrong further represented that "the people, **the marketplace**, and the customers now can feel with a great deal of certainty the commitment of AT&T . . . to . . . Excite At Home." *Id.* [Emphasis supplied.] (This uncertainty had been created, in large part, by AT&T's deceptive December 6, 1999 "open access" announcement.)

AT&T's foregoing assurances to the "marketplace" for At Home stock were grossly false and misleading. ¶63(b);JA2109. In fact, the March 28, 2000 agreements were an escalation in AT&T's ongoing efforts to take At Home's proprietary technology and customers. ¶¶59(t),60-65;JA2105,2107-2111. The only "commitment" reflected by such agreements was to buy-off the other control person customers so that AT&T would have clear sailing to misappropriate At Home's intellectual property, end its life, and take Cox and Comcast as customers of AT&T. ¶¶66,118(A)(2);JA2111-12,2141-42. Contrary to AT&T's assurance, these agreements were **not** a commitment by AT&T to the success of At Home. Consistent therewith, AT&T had no intention to enter, and did not enter, the new agreement with At Home, despite AT&T's representations to the contrary on March 29, 2000. ¶¶60-65,80,93;JA2107-11,2119,2129.

As the markets digested AT&T's deceptive statements and the accompanying SEC filings in late March and early April 2000, such statements caused the price of At Home stock to plummet by 60% over a four-week period. ¶59(t),118(A)(4); JA2105,2143.

The announcement of the March 28, 2000 Agreements, and the AT&T defendants' associated false assurances to the "marketplace," successfully accomplished the AT&T defendants' purpose to gain unfettered access to At Home's proprietary intellectual property. Immediately after this announcement, At Home began, according to its Chief Technology Officer, to give AT&T unfettered access to At Home proprietary technology (¶63(b);JA2109).

Moreover, defendants' deceptions also caused At Home shareholders to provide the necessary vote approving AT&T's purchase agreement transactions. In this regard, defendants failed to comply with SEC Item 404, 17 CFR § 229.404(a) when issuing At Home's May 28, 2000 Proxy **as well as in all other SEC filings** made during the Class Period. This SEC rule requires disclosure of related party transactions:

> *Transactions With Management and Others.* Describe briefly any transaction, or series of similar transactions, since the beginning of the registrant's last fiscal year, or any currently proposed transaction, or series of similar transactions, to which the registrant or any of its subsidiaries was or is to be a party, in which the amount involved exceeds $60,000, and in which any of the following persons had, or will have, a direct or indirect material interest . . . (1) Any director or executive officer of the registrant; (2) Any nominee for election as a director; (3) Any security holder who is known to the registrant to own more than five percent of any class of the registrant's voting securities . . .

AT&T's undisclosed nineteen takings of At Home's proprietary technology involved, in aggregate, more than $400,000,000 in At Home's property, including its proprietary technology, because that is what AT&T paid to settle the bankrupt At Home bondholders' claims of misappropriation. ¶110;JA2136. Each taking of At Home's proprietary technology, and the series of takings together, plainly represent a "transaction," as well as a series of transactions, of in excess of $60,000 between At Home and its "security holder who is known to own more than 5%" of At Home stock.

The failures to disclose the inherently deceptive act of control person misappropriation from the issuer constitute a clear violation of the applicable SEC rule designed to compel such disclosures.

d. AT&T's Continued Deceptive Statements Consummate Its Scheme

Once AT&T had obtained At Home shareholder approval of AT&T's control of At Home in September 2000, AT&T embarked on a series of steps to complete its takings of all of At Home's intellectual property, force At Home into bankruptcy, start AT&T's replacement network, effect a merger of part of AT&T and Comcast, and secure Cox and Comcast as new customers for AT&T's new network. ¶¶6,36,58,59(k)(6)-(11),69,70,72,91-107;JA2079,2086,2093,2097-102,2112-15,2126-35. The steps that weakened At Home and eventually forced At Home into bankruptcy included the withholding of revenues due to At Home by AT&T, Cox and Comcast; AT&T's causing At Home to overspend its budget; and AT&T's deceptive statement to At Home that AT&T would provide financing to At Home when, in fact,

AT&T had no such intention. ¶¶66,75(c)-(d),91(c)-(d),100;JA2111-12,2116-17,2127,2132-33.

As a direct result of AT&T's deceptive and associated steps pursuant to its scheme, At Home was compelled to enter into unfavorable ("death spiral") financing. ¶100;JA-2133. When announced on June 8, 2001, this caused a 52% drop in At Home's share price. *Id.* Ultimately, the AT&T defendants' scheme caused a total loss of the investment of those persons who purchased At Home stock and did not sell same.

5. Procedural History

In a series of orders from September 18, 2003 through August 9, 2004, reproduced at App. 46a-53a, the district court initially denied defendants' F.R.C.P. Rule 12(b)(6) motions to dismiss the Rule 10b-5 claims. After this Court's decision in *Dura Pharmaceuticals v. Broudo*, 544 U.S. 336 (2005), the court held that that portion of defendants' integrated scheme that was concealed by their misrepresentations could not comprise part of a scheme "in connection with the purchase or sale of securities" within the meaning of Rule 10b-5. App. 27a-29a. With the violative scheme reduced to merely the misrepresentations, the district court held that, under *Dura*, plaintiffs had failed to plead that their loss was caused by either a disclosure to the market of the misrepresentation or a materialization of the risk concealed by the misrepresentation. *Id.* 33a.

The Second Circuit affirmed by Order dated July 9, 2007 ("Order"). It held that the scheme was not "in connection with the purchase or sale of securities" under Rule 10b-5, *id.*, citing *Mutual Shares Corp. v. Genesco, Inc.*, 384 F.2d 540 (2d Cir. 1967). It also held, for

"substantially the reasons set forth by the district court," that plaintiffs had failed to plead loss causation from the misrepresentations. *Id.* 3a-4a.

REASONS FOR GRANTING THE PETITION

The scope of deceptive practices prohibited by § 10(b) is a recurring issue in the federal courts, including this Court. This Court granted certiorari in *Stoneridge Investment Partners v. Scientific-Atlanta, Inc.*, No. 06-43 ("*Stoneridge*"), to consider whether that scope extends to "deceptive devices and contrivances" by a defendant who makes no affirmative misrepresentations, but whose deceptive acts are concealed by and are part of an issuer's scheme and misrepresentations to the market.[6] *See also The Regents of the University of California v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 482 F.3d 372 (5th Cir. 2007), *petition for cert. filed* (April 5, 2007) (No. 06-1341) (raising virtually the same question of whether the scope of deceptive practices prohibited by §10(b) extends to non-speakers whose deceptive acts are concealed by and part of the issuer's misrepresentations to the market) ("*Regents*").

In conflict with *Stoneridge* and *Regents*, *Simpson v. AOL Time Warner, Inc.*, 452 F.3d 1040 (9th Cir. 2006), *petition for cert. filed* (Oct. 19, 2006) (No. 06-560) ("*Simpson*") held that deceptive practices of non-speakers are within the scope of acts prohibited by §10(b) where they further the scheme of an issuer who made misrepresentations to the market.

---

6. Petitioners believe that this case should be reviewed with *Stoneridge* to afford resolution of the closely related scheme liability issues. In the alternative, certiorari should be granted and this case held pending disposition of *Stoneridge*.

The Order constricts the scope of acts prohibited by §10(b) in a manner that conflicts with each of the Fifth, Eighth and Ninth Circuits and the prior rulings of this Court. The Order holds not only that must the violator make misrepresentations. Also, the violator's unlawful and deceptive acts concealed by those misrepresentations are excluded from the prohibition of Rule 10b-5 against a deceptive scheme or artifice "in connection with the purchase or sale of securities." This directly conflicts with the scope of prohibition found in *Simpson* and prior decisions of this Court. *SEC v. Zandford*, 535 U.S. 813 (2002); *Superintendent of Ins. of N.Y. v. Bankers Life & Casualty Co.*, 404 U.S. 6 (1971); *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972).

Similarly, the Order conflicts with the Exchange Act's requirements for proving loss causation and this Court's prior securities law causation decisions, including *Dura Pharmaceuticals v. Broudo*, 544 U.S. 336 (2005). Over three thousand cases have cited to *Dura*. A current and recurring issue of great importance in the federal securities laws is what private plaintiffs must allege in tracing loss causation from the violation to the decline in the share price.

Section 21D(b)(4) of the Exchange Act, 15 U.S.C. § 78u-4(b)(4), provides that a private plaintiff must prove "that the act or omission of the defendant alleged to violate this chapter caused the loss for which the plaintiff seeks to recover damages." By alleging that certain of the defendants' misrepresentations directly caused the price of the stock to decline, plaintiffs alleged facts that, if proved, complied with the implied requirements of

Section 21D(b)(4). In dismissing on loss causation grounds, the Order clearly conflicts with Section 21D(b)(4).

The Order also conflicts with *Dura*, which recognizes that where a misrepresentation causes a later act which, in turn, causes the stock price to decline, a private plaintiff satisfies loss causation. Here, plaintiffs alleged that defendants' scheme caused the stock price to decline and also caused other acts, which caused the stock price to decline. By holding that plaintiffs failed to meet the *Dura* standard for pleading loss causation, the Order conflicts with *Dura*.

This Court has recognized the need for certainty and predictability in the securities area, and the Second Circuit handles a large volume of securities cases. Granting the Petition to clarify the scope of prohibited conduct and the pleading of causation will resolve the conflict between the Order and all the foregoing authority on these important and recurring issues in securities law.

Granting certiorari also satisfies basic justice precepts of redressing injuries caused by fiduciaries who steal sensitive property from their beneficiary, lie to the market about their thefts, and also lie to the market about related matters in order to enable themselves to consummate their scheme to steal the most sensitive property and customers of their beneficiary.

As important as it may be to rein in some private actions under the federal securities laws, it is equally important that in the process egregious violations of Section 10(b) not be immunized. Granting certiorari will allow this Court to manage this process so as to maintain that balance.

I. IN CONFLICT WITH OTHER CIRCUITS, THIS COURT'S OWN PRIOR DECISIONS, AND THE PLAIN LANGUAGE OF RULE 10b-5, THE ORDER EFFECTIVELY LIMITS THE SCOPE OF CONDUCT PROHIBITED BY RULE 10b-5 SOLELY TO MISREPRESENTATIONS

A. Conflicts With Prior Decisions Of This Court

The Order held that only defendants' misrepresentations were in connection with the purchase or sale of securities within the meaning of Rule 10b-5, and that the deceptive and unlawful acts that the misrepresentations concealed were not in connection with the purchase or sale of securities. App. 3a (court of appeals opinion); *id.* 25a-29a (district court opinion).

This holding conflicts with prior decisions of this Court. *SEC v. Zandford*, 535 U.S. 813 (2002) (deception created by breach of fiduciary duty to disclose sales of securities and conversion of proceeds constitutes scheme in connection with purchase or sale of securities); *Superintendent of Ins. of N.Y. v. Bankers Life & Casualty Co.*, 404 U.S. 6 (1971).

Where misrepresentations conceal breaches of fiduciary duty, such breaches are part of the fraud in connection with the purchase or sale of securities. *E.g.*, *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972) (misstatements of material fact used by bank employees in position of market maker to acquire stock at less than fair value); *Superintendent*, (seller (of bonds) was duped into believing that it, the seller, would receive the proceeds). *Cf. SEC v. Capital Gains Research*

Bureau, 375 U.S. 180 (1963) (injunction under Investment Advisers Act of 1940 to compel registered investment adviser to disclose to his clients his own financial interest in his recommendations). *Compare Santa Fe Indus. v. Green*, 430 U.S. 462 (1977) (where no misrepresentation is alleged, mere breach of fiduciary duty did not violate Rule 10b-5).

In *Zandford*, the Court emphasized that "neither the SEC nor this Court has ever held that there must be a misrepresentation about the value of a particular security in order to run afoul of the Act." 535 U.S. at 820. There a broker's sale of his customers' securities with the undisclosed intent to misappropriate the proceeds constituted a fraudulent scheme "in connection with the purchase or sale of any security."

> [E]ach sale was made to further respondent's fraudulent scheme; each was deceptive because it was neither authorized by, nor disclosed to, the Woods. . . . Indeed, each time respondent 'exercised his power of disposition for his own benefit,' **that conduct, 'without more,' was a fraud**. . . .
>
> . . . . The fact that respondent misappropriated the proceeds of the sales provides persuasive evidence that he had violated § 10(b) when he made the sales, **but misappropriation is not an essential element of the offense. . . . It is enough that the scheme to defraud and the sale of securities coincide.**

Id. at 820-23 (citations omitted) (emphasis supplied). *Zandford* concerned neither misrepresentations nor

omissions, but deceptive conduct. Here, far more than in *Zandford*, the violator engaged in affirmative misrepresentations that "we protect" the IP in order to enable itself to misappropriate such IP through these and other escalating misrepresentations and deceptions in an integrated scheme or artifice. *See* Statement of the Case *supra*. This scheme inflated the market price of At Home stock and, thus, satisfied the "in connection with" test in a way that *Zandford* did not. *See Zandford*, 535 U.S. at 822 (inflation of publicly traded securities prices sufficient though not necessary to satisfy the "in connection with" test). Thus, the Order directly conflicts with *Zandford* in this respect.

Moreover, one of the deceptions that the violator used to misappropriate the IP here successfully induced shareholder approval of AT&T's purchase of control blocks of stock of At Home owned by Cox and Comcast. *See* Statement of the Case *supra*. This purchase increased AT&T's control over At Home to the following point: At Home's most sensitive IP, which At Home had previously resisted turning over to AT&T, was then provided to the omnipotent AT&T. This "coinciding" of the scheme and the purchase or sale of securities was what satisfied and was "enough" to satisfy the "in connection with" test in *Zandford*. Here, also, AT&T's scheme employed AT&T's purchase of securities, **and shareholder approval thereof**, to effect the scheme. Even more than in Zandford, such scheme or artifice was in connection with the purchase and sale of securities. This constitutes a second conflict between the Order and *Zandford*.

Third, the Order appears to hold that "nothing in the SEC regulations required that defendants disclose the misappropriation scheme." App. 4a (court of appeals); *see id.* 26a, 31a (district court). However, SEC Regulation S-K, Item 404(a), 17 CFR § 229.404(a), as then in effect expressly required disclosure of related party transactions as follows:

> *Transactions With Management and Others.* Describe briefly any transaction, or series of similar transactions, since the beginning of the registrant's last fiscal year, or any currently proposed transaction, or series of similar transactions, to which the registrant or any of its subsidiaries was or is to be a party, in which the amount involved exceeds $60,000, and in which any of the following persons had, or will have, a direct or indirect material interest . . . (1) Any director or executive officer of the registrant; (2) Any nominee for election as a director; (3) Any security holder who is known to the registrant to own more than five percent of any class of the registrant's voting securities . . .

Thus, even more than in *Zandford*, the misappropriation here triggered an explicit SEC disclosure requirement designed to inform prospective or actual shareholders about any looting or improper transactions by insiders of an issuer of public stock. *Zandford* merely involved general fiduciary principles. Clearly, the unlawful scheme here was, *in toto*, in connection with the purchase or sale of securities. This constitutes a third conflict between the Order and *Zandford*.

Zandford relied upon *Superintendent*. There the directors of Manhattan Casualty Company authorized the sale of treasury bonds because they had been "duped" into believing that the company would receive the proceeds of the sale. 404 U.S. at 9. The Court held that "Manhattan was injured as an investor through a deceptive device which deprived it of any compensation for the sale of its valuable block of securities." *Id.*, at 10. The Court explicitly rejected the Second Circuit's narrow reading of § 10(b) in *Superintendent of Ins. of N.Y. v. Bankers Life & Casualty Co.*, 430 F.2d 355, 361 (2d Cir. 1970),[7] that because the fraud against Manhattan did not occur on a securities exchange, it was not prohibited by § 10(b). 404 U.S. at 10. Noting that § 10(b) "must be read flexibly, not technically and restrictively," *id.* at 12, the Court stated that while the interest in "preserving the integrity of the securities markets" was one of the purposes of the statute, it was not limited to that objective. *Id.*

Here, At Home stock was traded on the Nasdaq and the "integrity of the market" test is satisfied, though it is not necessary to satisfaction of the "in connection with" test. However, relying on *Mutual Shares Corp. v.*

7. This Court again found fault with the Second Circuit's narrow reading of § 10(b)'s "in connection with" language in *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, 547 U.S. 71, 85 (2006) ("Under our precedents, it is enough that the fraud alleged 'coincide' with a securities transaction – whether by the plaintiff or by someone else. The requisite showing, in other words, is 'deception "in connection with the purchase or sale of any security," not deception of an identifiable purchaser or seller.'") (citations omitted).

Genesco, Inc., 384 F.2d 540 (2d Cir. 1987), the district court determined below that

> the scheme alleged here involved corporate abuse, misconduct and diversion of assets, but no transactions in the relevant securities. Its success depended on the misappropriation of At Home's proprietary technology, without regard to any transactions in At Home stock. . . .
>
> The PTAC does allege that in March 2000 AT & T increased its control over At Home by acquiring At Home shares from Cox and Comcast in exchange for AT & T shares. However, an otherwise legitimate stock transaction that is antecedent, but not integral, to the alleged fraud does not meet the 'in connection with' requirement. *See Zandford*, 535 U.S. at 820, 122 S.Ct. 1899 (neither an otherwise legitimate securities transaction that is an independent event from the alleged fraud, or is merely followed by the theft of the proceeds of the transaction, supports a claim under Section 10(b)). Indeed, the defendants in *Mutual Shares*, like AT & T here, acquired a controlling position in the issuer before carrying out their scheme, 384 F.2d at 542, but the Court of Appeals nevertheless dismissed plaintiffs' claim based on the subsequent diversion of assets from the issuer. *Id.* at 546.

App. 27a-28a. The district court's above "finding" is contrary to the plain allegations of the complaint that the integrated scheme had gone on for six months **before**

AT&T had to escalate the scheme. AT&T then made expensive purchases of At Home stock in order to misappropriate the most sensitive IP from At Home, which had theretofore resisted divulging same.

Also, in *Mutual Shares*, plaintiffs alleged that defendants, as part of the tender offer through which they would become controlling shareholders of a public company, defrauded them by remaining silent as to (1) their true intentions to manage the acquired company for their benefit, and (2) the actual (higher) value of real estate owned by the acquired company. 384 F.2d at 544. Plaintiffs were not sellers to defendants in the tender offer but were purchasers (at allegedly depressed prices) who continued to hold their shares, and who **failed to allege that defendants had any non-public information as to the value of the real estate.** *Id.* at 544-45. The Court characterized the secret intention to abuse the acquired company as a "failure to disclose by an outsider," or "at best" an allegation "that defendants impliedly represented to the world at large that they would not mismanage [the acquired company] if they acquired control and that plaintiffs relied on this when they bought their . . . stock. Plaintiffs cite no cases in which [Rule 10b-5] has been applied in this expansive manner, nor have we been able to find any." *Id.* at 545 (footnote omitted).

In contrast, AT&T was an insider and control person which was misappropriating IP and falsely stating that the IP was protected **at the same time** that it was engaged in other misrepresentations to enable it to misappropriate the IP. Only after its scheme had long been under way, did AT&T purchase additional control

blocks of At Home stock on false pretenses in order to enable it to misappropriate the most sensitive parts of At Home's IP. AT&T's undisclosed and unlawful scheme had been inflating the prices of At Home stock paid by plaintiffs long before AT&T engaged in its lies to induce shareholder approval of AT&T's purchase of the control block of At Home's stock. Thus, *Mutual Shares* is extremely distinguishable.

Similarly, the Order conflicts with other decisions of this Court insofar as the Order severed the deceptive and unlawful acts concealed by the misrepresentations from the integrated scheme or artifice. Having thus severed these deceptive acts, the Order erroneously held that they are not prohibited by Section 10(b). But prior decisions of this Court hold to the contrary. *Affiliated Ute Citizens*; *SEC v. Capital Gains Research Bureau*, 375 U.S. 180 (1963). Certiorari should be granted to resolve all of the foregoing conflicts between this Court's prior decisions and the Order.

B. The Order Conflicts With The Plain Language Of The Statute And Rule

Under the plain language of the statute, defendants' integrated scheme or artifice, *in toto*, constitutes a violation of the statute "in connection with" plaintiffs' purchases and sales of At Home's securities as well as AT&T's purchases. Under extensive precedent of this Court, it is incorrect to dumb down "scheme" or "artifice" violations into merely the "misrepresentation."

Thus, the Order further conflicts with this Court's clear precedent that statutes be interpreted in accordance with their plain language.

This Court has often stated that it will rely on the text of the statute to determine the scope of rights and remedies under the Exchange Act. For example, in granting certiorari in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 508 U.S. 959 (1993), the Court *sua sponte* directed the parties to brief the question "[w]hether there is an implied private right of action for aiding and abetting violations of Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5." In holding that there was no such implied right of action, the Court relied almost exclusively on the text of Section 10(b), which does not reach actors who aid and abet a violation of the section by another.

> With respect . . . to . . . the scope of conduct prohibited by § 10(b), the text of the statute controls our decision. . . . We have refused to allow 10b-5 challenges to conduct not prohibited by the text of the statute.

Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A., 511 U.S. 164, 173 (1994).[8] *See also Santa*

8. The Court further noted that

> [t]he absence of § 10(b) aiding and abetting liability does not mean that secondary actors in the securities markets are always free from liability under the securities Acts. Any person or entity, including a lawyer, accountant, or bank, who employs a manipulative device or makes a material misstatement (or omission) on which a purchaser or seller of securities relies may be liable as a primary violator under 10b-5, assuming *all* of the requirements for primary liability under Rule 10b-5 are met.

511 U.S. at 191.

Fe Indus., 430 U.S. at 472-74; *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 197 (1976) ("In addressing [the elements of a cause of action under Section 10(b) and Rule 10b-5], we turn first to the language of § 10(b), for '[t]he starting point in every case involving construction of a statute is the language itself.'" (quoting *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 756 (1975) (Powell, J., concurring))).

Moreover, a "statute must, if possible, be construed in such fashion that every word has some operative effect." *United States v. Nordic Village, Inc.*, 503 U.S. 30, 36 (1992). *See also Duncan v. Walker*, 533 U.S. 167, 174 (2001) ("It is our duty to give effect, if possible, to every clause and word of a statute."). Here the critical language of § 10(b) makes it unlawful "for any person, directly or indirectly . . . [t]o use or employ . . . any . . . deceptive device or contrivance." The Court has understood "device" to mean "that which is devised, or formed by design; a contrivance; an invention; project; scheme; often, a scheme to deceive; a stratagem; an artifice." "Contrivance," according to the Court, means "a thing contrived or used in contriving; a scheme, plan or artifice." *Hochfelder*, 425 U.S. at 199 n. 20 (quoting Webster's New International Dictionary 580, 713 (2d ed. 1934).

In construing the "in connection with" language of Section 10(b) and Rule 10b-5 to extend only to certain misrepresentations, the Order conflicts with Congress' plain language and prior decisions of this Court interpreting this language.

Moreover, numerous decisions of this Court make clear that Section 10(b) "should be 'construed not technically and restrictively, but flexibly to effectuate its remedial purposes.'"[9] Flexible construction of the plain language of the statute does not permit a narrow interpretation which would require, absent textual support, that a "deceptive device or contrivance" be permitted when Congress and the SEC have prohibited same. The Order conflicts with the prior decisions of this Court in this respect as well.

C. Conflict With Other Circuits

In each of three recent circuit court decisions construing the scope of conduct prohibited by Rule 10b-5, the court held that deceptive acts could constitute, together with misrepresentations, a scheme or deception in violation of Rule 10b-5.

In *Simpson*, plaintiffs alleged that defendants engaged in a scheme to overstate the reported revenues of Homestore.com by entering into sham transactions in which payments were made to Homestore, which then returned monies to the "vendors."

> We conclude that conduct by a defendant that had the principal purpose and effect of creating a false appearance in deceptive

9. *E.g.*, *Zandford*, 535 U.S. at 819, quoting *Affiliated Ute Citizens*, 406 U.S. at 151 (internal quotation marks omitted); *accord*, *Pinter v. Dahl*, 486 U.S. 622, 653 (1988); *Herman & MacLean v. Huddleston*, 459 U.S. 375, 386-87 (1983); *Santa Fe Indus.*, 430 U.S. at 475-76; *Superintendent*, 404 U.S. at 12; *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963).

> transactions as part of a scheme to defraud is conduct that uses or employs a deceptive device within the meaning of § 10(b). Furthermore, such conduct may be in connection with the purchase or sale of securities if it is part of a scheme to misrepresent public financial information where the scheme is not complete until the misleading information is disseminated into the securities market. Finally, a plaintiff may be presumed to have relied on this scheme to defraud if a misrepresentation, which necessarily resulted from the scheme and the defendant's conduct therein, was disseminated into an efficient market and was reflected in the market price.

452 F.3d at 1050-52. The court affirmed the dismissal of Rule 10b-5 claims but remanded to allow plaintiffs to seek leave to replead under the new standard. *Id.* at 1048.

By limiting the scope of conduct prohibited by Rule 10b-5 to misrepresentations, and by further excluding deceptive conduct from consideration as part of a scheme to defraud, the Order directly conflicts with the Ninth Circuit's decision in *Simpson*.

The scope of conduct prohibited by Rule 10b-5 is currently before this Court in *Stoneridge*. There, the Eighth Circuit refused to hold non-speaking defendants liable under § 10(b) for a course of business whose sole purpose was to allow a public company to report falsely inflated earnings. In so limiting the scope of prohibited conduct, the Eighth Circuit adopted a "bright line" test:

> [A]ny defendant who does not make or affirmatively cause to be made a fraudulent statement or omission, or who does not directly engage in manipulative securities trading practices, is at most guilty of aiding and abetting and cannot be held liable under § 10(b) or any subpart of Rule 10b-5.

443 F.3d at 992.

In *Regents*, the Fifth Circuit adopted the Eighth Circuit's bright line test, requiring misrepresentations or omissions in a private § 10(b) action. Defendant were alleged to have participated in transactions which allowed Enron Corp. to take liabilities off its books temporarily and to book revenues from transactions when it was actually incurring debt. The Fifth Circuit cited the split between the Eighth and Ninth Circuits on the issue of scheme liability in the absence of misrepresentation, aligning itself with the Eighth Circuit in *Stoneridge*.

> An act cannot be deceptive within the meaning of § 10(b) where the actor has no duty to disclose. . . .
>
> [T]he Court, in its . . . cases interpreting § 10(b), has established that a device, such as a scheme, is not 'deceptive' unless it involves breach of some duty of candid disclosure.

482 F.3d at 386, 389 (citations and footnotes omitted). However, neither *Stoneridge* nor *Regents* went so far as to exclude the deceptive non-speaking conduct

altogether from the scope of prohibited activity. In doing so, the Order goes far beyond and conflicts with *Stoneridge* and *Regents* as well. Granting certiorari is necessary to resolve the foregoing conflicts on the recurring and important issue of the scope of conduct prohibited by Section 10(b).

II. THE ORDER'S LOSS CAUSATION RULING CONFLICTS WITH 15 U.S.C. § 78u-4(b)(4) AND THE PRIOR DECISIONS OF THIS COURT

A. Conflict with 15 U.S.C. § 78u-4(b)(4)

An additional issue of recurring importance calling for resolution in this case is the conflict between the Order and the text of the Exchange Act setting forth the requirements of proving loss causation. Congress provided that:

> In any private action arising under this chapter, the plaintiff shall have the burden of proving that **the act** or omission **of the defendant alleged to violate this chapter caused the loss** for which the plaintiff seeks to recover damages.

Section 21D(b)(4) of the Exchange Act, 15 U.S.C. § 78u-4(b)(4) (emphasis supplied); App. 57a.

Here, plaintiffs expressly alleged that certain of defendants' misrepresentations on December 6, 1993 and March 29, 2000 directly caused the price of the stock of At Home to decline. *See* Statement of Case *supra*. If proved, these allegations satisfy Section 21D(b)(4). In

holding against plaintiffs, neither the Order nor the district court ever mentioned these misrepresentations that directly decreased the price of At Home stock. Whether intentionally or by inadvertence, the Order, in rejecting loss causation based on these misrepresentations, clearly conflicts with the implied pleading requirement of Section 21D(b)(4).

In this regard, the plain language of Section 21D(b)(4) controls. *See Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 197 (1976), and cases collected at Point I.A. *supra*. The text of §21D(b)(4) does not specify a burden of proving causation from a "statement or omission" or a "misrepresentation or omission," but rather from an "act or omission." Congress thus clearly contemplated that "the act . . . of the defendant alleged to violate this chapter" could include not merely the "act of speaking" but also "any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person," as set forth in Rule 10b-5(c). *See* Point I.A. *supra*.

Absolutely nothing in the statutory text suggests that employment of a "deceptive device or contrivance" in connection with the purchase or sale of securities be limited only to instances where a misrepresentation accompanies the conduct. In this context, plaintiffs separately satisfied §21D(b)(4) by alleging that the violator's deceptions caused other acts (desperation financing) that caused the price of At Home stock to fall. *See* Statement of Case *supra*. By holding to the contrary, the order further conflicts with §21D(b)(4).

Finally, plaintiffs also argued below that they satisfied loss causation by pleading a leak of the truth and the materialization of the concealed risk in numerous respects.

B. Conflict With The Prior Decisions Of This Court

This Court has recognized that "[t]here is . . . more than one way to demonstrate the causal connection" for purposes of Rule 10b-5. *Basic, Inc. v. Levinson*, 485 U.S. 224, 243 (1988). Specifically with regard to loss causation, this Court has held that, in a pure misrepresentation case, causation is adequately pleaded where a misrepresentation allegedly causes a later leak or corrective disclosure that, in turn, causes a decline in the stock price. *Dura*, 544 U.S. at 347. *Dura* specifically relied on common law proximate cause. 544 U.S. at 345. Where intentional harm or injury is alleged, the common law is astute to find causation of injury at the pleading stage.[10]

---

10. In *Dura*, this Court cited (twice) to W. Page Keeton, PROSSER & KEETON ON THE LAW OF TORTS § 8 at 37 n. 27 (5th ed. 1984) as an authoritative source of common law proximate cause principles. PROSSER quotes from *Derosier v. New England Tel. & Tel. Co.*, 130 A. 145, 152 (N.H. 1925) (emphasis supplied) as follows:

> In determining how far the law will trace causation and afford a remedy, the facts as to defendant's intent, his imputable knowledge, or his justifiable ignorance are often taken into account. The moral element is the factor that has turned close cases one way or another. **For an intended injury, the law is astute to discover even very remote causation.** For one which the

(Cont'd)

Per force, where, as here, plaintiff explicitly alleges that the misrepresentations themselves intentionally caused the decline in the price of the stock, loss causation is adequately pleaded under *Dura* and 15 U.S.C. § 78u-4(b)(4) *supra*. The Order clearly conflicts with *Dura* in this respect.

Similarly, in a scheme case, where the scheme or deceptive acts caused other acts—here including desperation financing—that caused the decline in stock price, loss causation is adequately pleaded under *Dura*'s reasoning. In holding to the contrary, the Order once again directly conflicts with *Dura*.

III. OTHER REASONS FOR GRANTING THE PETITION

Liability under the Exchange Act is "an area that demands certainty and predictability" for those who provide services to participants in the securities business. *E.g.*, *Pinter v. Dahl*, 486 U.S. 622, 652 (1988). The Second Circuit handles a high proportion of actions filed under the federal securities laws. This case presents the opportunity for this Court to provide certainty and predictability regarding the previously demonstrated conflicts in the "in connection with" and the loss causation standards in the context of scheme liability.

(Cont'd)

> defendant merely ought to have anticipated it has often stopped at an earlier stage of the investigation of causal connection. And as to those where there was neither knowledge nor duty to foresee, it has usually limited accountability to direct and immediate results.

Granting certiorari also satisfies basic justice precepts of redressing injuries caused by fiduciaries who steal sensitive property from their beneficiary, lie to the market about their thefts, and also lie to the market about related matters in order to enable themselves to consummate their scheme to steal the most sensitive property and customers of their beneficiary.

As important as it may be to rein in some private actions under the federal securities laws, it is equally important that in the process egregious violations of Section 10(b) not be immunized. Granting certiorari here will allow this Court to manage this process so as to maintain that balance.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

CHRISTOPHER LOVELL
Counsel of Record
GARY S. JACOBSON
IAN T. STOLL
LOVELL STEWART HALEBIAN LLP
500 Fifth Avenue
New York, New York 10110
(212) 608-1900

Counsel for Petitioners

APPENDIX A — SUMMARY ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT FILED JANUARY 30, 2007

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

No. 06-1583-cv

Semen LEYKIN, on behalf of himself and all others similarly situated,

Plaintiffs-Appellants,

FRANK THOMAS, KEN PEARLMAN, MIKE KATTO, AT HOME SUIT GROUP, INC., KURT BUETTLER, GERRY GALIGER, STAN COHN, CHANNA UNGER, MICHAEL EKSLER, FREIDA EKSLER and RONALD VENTURA,

Consolidated Plaintiffs-Appellants,

v.

AT & T CORPORATION, KLEINER, PERKINS CAUFIELD & BYERS, C. MICHAEL ARMSTRONG, MARK MCEACHEN, FRANK IANNA, CHARLES H. NOSKI, DANIEL H. SOMERS, JOHN C. PETRILLO, JOHN C. MALONE, EDWARD S. ROGERS, DAVID M. WOODROW, HOSSEIN ESLAMBOLCHI, BRIAN L. ROBERTS, RAYMOND LIGUORI, THOMAS A. JERMOLUK, WILLIAM R. HEARST III and L. JOHN DOERR,

Defendants-Appellees,

Appendix A

COX COMMUNICATIONS, INC., COMCAST CABLE COMMUNICATIONS, INC. and MOHAN GYANI,

Consolidated-Defendants-Appellees,

PATTI HART and MUFIT CINALI,

Defendants.

Present:

AMALYA L. KEARSE,
HON. ROBERT A. KATZMANN,
Circuit Judges,
DAVID G. TRAGER,
*District Judge.**

SUMMARY ORDER

Appeal from the United States District Court for the Southern District of New York (Stanton, *J.*).

On consideration whereof, it is hereby **ORDERED, ADJUDGED,** and **DECREED** that the orders of the district court, dated September 17, 2003, August 9, 2004, and March 23, 2006 (as amended on June 28, 2006), be and they hereby are **AFFIRMED.**

---

* The Honorable David G. Trager, District Judge, United States District Court for the Eastern District of New York, sitting by designation.

Appendix A

Plaintiffs-appellants appeal the order dismissing their first amended complaint ("FAC") and denying them leave to file second and third amended complaints. These three complaints all alleged, in pertinent part, that the defendants violated Sections 10(b), 14(a), and 20(a) of the Securities Exchange Act and the regulations promulgated thereunder, as well as committed common law fraud and breach of fiduciary in violation of Delaware law. *See* 15 U.S.C. § § 78j(b), 78n, 78t(a); 17 C.F.R. §§ 240.10b, 240.14a-9. We assume the parties' familiarity with the facts, the proceedings below, and the specification of issues on appeal.

The primary thrust of the plaintiffs' complaint is that the AT & T defendants engaged in a secret scheme to convert At Home's proprietary technology and that this scheme, as well as misrepresentations related to it, led to a decline in the price of At Home's stock. To state a claim under § 10(b) and Rule 10b-5, plaintiffs must allege (1) a material misrepresentation (or omission), (2) scienter, (3) a connection with the purchase or sale of a security, (4) reliance, (5) economic loss, and (6) loss causation. *Dura Pharms., Inc. v. Broudo*, 544 U.S. 336, 341-42, 125 S.Ct. 1627, 161 L.Ed.2d 577 (2005). For substantially the reasons set forth by the district court, *see Leykin v. AT & T Corp.*, 423 F. Supp. 2d 229 (S.D.N.Y. 2006), the plaintiffs here have failed to allege that the AT & T defendants' conversion scheme was in connection with the purchase or sale of securities, *see, e.g., Mutual Shares Corp. v. Genesco, Inc.*, 384 F.2d 540, 545-46 (2d Cir. 1967), and that any misrepresentation associated with that scheme was the cause of plaintiffs' loss under

the standard set forth in *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. at 346-47, 125 S.Ct. 1627.

As to plaintiffs' claims under § 14(a), an "[o]mission of information from a proxy statement is actionable if either the SEC regulations specifically require disclosure of the omitted information in a proxy statement, or the omission makes other statements in the proxy statement materially false or misleading." *Seinfeld v. Gray*, 404 F.3d 645, 650 (2d Cir.2005) (internal quotation marks omitted). Here, nothing in the SEC regulations required that defendants disclose the AT & T defendants' misappropriation scheme, and that omission did not "make[ ] other statements in the proxy statement materially false or misleading." *Id.* Because plaintiffs have failed to allege primary violations of § 10b or § 14(a), their claims of control person liability under § 20(a) must also fail. *See, e.g., Boguslavsky v. Kaplan*, 159 F.3d 715, 720 (2d Cir.1998) (holding that to bring a claim under § 20(a), a plaintiff must show, *inter alia*, "a primary violation by a controlled person").

Finally, plaintiffs' claims for common law fraud and breach of fiduciary duty of candor toward the shareholders are preempted by the Securities Litigation Uniform Standards Act, which provides that "[n]o covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging . . . a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security." 15 U.S.C. § 78bb(f)(1).

Appendix A

We have considered all of plaintiffs-appellants' other arguments and find them without merit. Accordingly, for the foregoing reasons, the judgment of the district court is hereby **AFFIRMED.**

FOR THE COURT:
THOMAS ASREEN, ACTING CLERK

By: s/ Lucille Carr

APPENDIX B — OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK DATED MARCH 23, 2006, AS AMENDED JUNE 26, 2006

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

No. 02 Civ. 1765 (LLS)
AND ALL CONSOLIDATED
AND RELATED ACTIONS

SEMEN LEYKIN, on behalf of himself and all others similarly situated,

Plaintiff,

- against -

AT & T CORPORATION; COX COMMUNICATIONS, INC.; COMCAST CABLE COMMUNICATIONS, INC.; KLEINER PERKINS CAUFIELD & BYERS; C. MICHAEL ARMSTRONG; MARK MCEACHEN; GEORGE BELL; FRANK IANNA; MOHAN GYANI; CHARLES H. NOSKI; DANIEL H. SOMERS; JOHN C. PETRILLO; L. JOHN DOERR; THOMAS A. JERMOLUK; WILLIAM R. HEARST, III; RAYMOND LIGUORI; JOHN C. MALONE; BRIAN L. ROBERTS; EDWARD S. ROGERS; DAVID M. WOODROW; and HOSSEIN ESLAMBOLCHI,

Defendants.

Appendix B

OPINION AND ORDER

In these consolidated and related securities class actions, defendants move to dismiss the first amended (and predecessor) complaints and the proposed third amended complaint ("PTAC"), which plaintiffs tender as their best statement of "loss causation."

FACTS

The facts set forth below are taken from the PTAC, the documents referenced therein and publicly available financial filings. *Rothman v. Gregor*, 220 F.3d 81, 88 (2d Cir.2000). The facts are presumed to be true for purposes of this motion. *Papasan v. Allain*, 478 U.S. 265, 283, 106 S.Ct. 2932, 2943, 92 L.Ed.2d 209 (1986).

1. At Home and its Proprietary Technology

In 1995, defendant Kleiner Perkins Caufield & Byers, a venture-capital partnership, and Tele-Communications, Inc. ("TCI"), a cable television company, co-founded an Internet services company named At Home Corporation. At Home developed and managed complex computer software and systems that enabled customers with a personal computer and a cable modem to gain access to the Internet at high speeds over existing television cable lines (the "proprietary technology"). (PTAC ¶ 2(a),(b).) It repeatedly represented that it regarded its technology as proprietary and that it attempted to protect its rights therein. *Id.* at ¶ 4.

2. At Home's Cable Partners

In 1996, TCI and two other cable companies, Cox Communications, Inc. and Comcast Cable Communications, Inc., entered Master Distribution Agreements ("MDAs") with At Home, which required them to use only At Home's service to provide high-speed Internet access to their cable television subscribers through June 4, 2002. (PTAC ¶ 49.) Pursuant to those agreements, the cable companies paid At Home 35% of the average $45 monthly subscription fee per customer to provide high-speed Internet access to those customers. *Id.* at ¶ ¶ 3, 49. In addition, Cox and Comcast each acquired stock in At Home and began offering At Home's high-speed Internet service to their cable television markets. *Id.* at ¶ ¶ 50, 52, 54(c).

In June 1998, AT & T Corporation announced that it would acquire TCI, including its controlling interest in At Home, in hopes of using At Home's proprietary technology to provide residential video, voice and data services on a single platform, something no other company had been able to do. *Id.* at ¶ 55. The merger was finalized in March 1999, and TCI was renamed AT & T Broadband, LLC. *Id.* at ¶ 58.

In December 1998, pursuant to an Indefeasible Right to Use Capacity Agreement ("IRU"), AT & T sold At Home the exclusive right to use AT & T's private fiber optic data network. The IRU enabled At Home to provide high-speed Internet service to millions of users without having to build its own network. *Id.* at ¶ 57. At Home

and AT & T touted this agreement as enabling At Home to expand its services for years to come. *Id.*

3. Misappropriation of At Home's Technology

On November 8, 1999, the day before the start of the class period, At Home's stock price closed at $44.94. (PTAC ¶ 8.) However, that price did not reflect a secret plan AT & T had devised to duplicate At Home's network so it could provide high-speed Internet service on its own. To carry out its scheme, between August 1999 and August 28, 2001 AT & T demanded, gained access to and copied all of At Home's proprietary technology, even though it had no contractual right to do so. *Id.* at ¶¶ 59(d),(h),(s), 110(b). AT & T also refused to make a non-disclosure or non-compete agreement with At Home. *Id.* at ¶ 87.

A significant element of AT & T's plan to misappropriate At Home's proprietary technology was a program known as Open Access, which was first announced on December 6, 1999. The ostensible purpose of the program was to offer AT & T's customers a choice between several Internet service providers, rather than only the At Home service. *Id.* at ¶ ¶ 59(k), 67. Although that choice was never actually offered during the class period, AT & T demanded that At Home turn over virtually all of its proprietary technology, stating that it was needed for tests in preparation for Open Access. In reality, AT & T's demands for At Home's proprietary technology went far beyond what was necessary to conduct such tests. *Id.* at ¶ 59(k). Those demands caused

"many At Home employees to leave the Company for various reasons, specifically including the suspicion that AT & T was attempting, in reality, not to conduct any tests but to take At Home's proprietary technology"*id.* at ¶ 59(k)(1) as well as "tremendous dissent and distraction during At Home's board meetings for the remainder of At Home's existence." *Id.* at ¶ 59(k)(3).

The Open Access announcement did not disclose AT & T's misappropriation. *Id.* at ¶ 59(k). Indeed, the conversion of At Home's technology was never disclosed to the market during the class period. *Id.* at ¶ 86. Nor did AT & T's misappropriation of At Home's technology diminish the technology's usefulness. *Id.* at ¶ 6.

4. March 2000 Agreements

At Home made a series of agreements with AT & T, Cox and Comcast on March 28, 2000. The first was a control agreement whereby AT & T acquired all of Cox and Comcast's At Home stock in exchange for shares of AT & T. That gave AT & T a 74% voting interest and a 23% economic interest in At Home, as well as the ability to appoint a majority of its board. Cox and Comcast agreed to resign their seats on At Home's board. (PTAC ¶¶ 61(b), 70(b).)

The March 2000 Agreements also gave Cox and Comcast the option of terminating the exclusivity provisions of the 1996 MDAs with At Home, or the 1996 MDAs entirely, as early as June 2001-a year earlier than they were originally scheduled to expire. *Id.* at ¶ 61(c).

Cox and Comcast also obtained the right to acquire components of At Home's technology, which would enable them to offer aspects of At Home's service themselves. *Id.* at ¶ 61(d).

AT & T, Cox and Comcast also represented that they would, as promptly as practicable, execute new non-exclusive MDAs to govern their relationships with At Home through 2006. Despite those representations, no new MDAs were made. *Id.* at ¶¶ 59(t), 62, 75(e). In addition, Cox and Comcast, who together provided approximately 25% of At Home's revenues, *id.* at ¶ 75(c), informed At Home as early as September 2000 and April 2001, respectively, that they intended to provide high-speed Internet service themselves and end their relationships with At Home. *Id.* at ¶ 71-75, 102. On June 19, 2001, they each notified At Home that they would exercise their rights under the March 2000 agreements to terminate the exclusivity provisions of their 1996 MDAs, effective December 4, 2001. *Id.* at ¶ 102.

5. Promethean Financing and IRU Recapture Agreement

During the spring and summer of 2001, At Home was experiencing financial problems. (PTAC ¶ 98.) AT & T initially agreed to provide At Home with funding, but reneged when At Home refused to turn over more of its proprietary technology. *Id.* at ¶ 105. At Home was then forced to issue and sell $100 million of zero-percent five-year convertible secured notes in a private offering arranged by Promethean Capital Group, LLC on or

about June 8, 2001 ("Promethean Financing"). *Id.* at ¶ 100. At Home was also forced to sell certain rights under the IRU back to AT & T on June 19, 2001 for $75 to $85 million, although At Home experts had determined that those rights had a fair market value of approximately $130 million. *Id.* at ¶ ¶ 89, 90. At Home's stock price declined from $3.92 on June 8, 2001 to $1.90 on June 19, 2001. *Id.* at ¶ 100.

6. At Home's Bankruptcy

On July 23, 2001, At Home filed an S-3 Registration Statement in connection with the Promethean Financing, which stated "We will need to raise additional funds before the end of 2001 to support our business operations. If we are unsuccessful at raising funds, this could have a material adverse impact on our operations and liquidity."(PTAC ¶ 106.)

Less than a month later, At Home announced in its Form 10-K/A filed on August 20, 2002 that there was "substantial doubt about our ability to continue as a going concern" and that "We cannot guarantee that we will be able to obtain additional funding on acceptable terms, if at all." *Id.* at ¶ 107. On August 30, 2001, At Home announced that it could not repay the Promethean loan due the next day. *Id.* at ¶ 109. On September 28, 2001, At Home sold substantially all of its Internet business assets to AT & T and filed for bankruptcy. *Id.* at ¶ 110(a), (b). By that date, the price of At Home's stock had fallen to $0.15. (Winter Sept. 6, 2005 Aff. Ex. 28.)

Finally, in December 2001, At Home stopped servicing AT & T pursuant to a bankruptcy court order and AT & T stopped paying At Home. (PTAC ¶ 111.) AT & T then canceled its September 28, 2001 purchase of At Home's assets. *Id.* With the use of At Home's proprietary technology it had finished taking three months earlier, AT & T then began servicing customers on its own network, which today services both Cox and AT & T Broadband/Comcast[1] subscribers. *Id.* at ¶¶ 6, 111.

PROCEDURAL HISTORY

On November 7, 2002, plaintiffs filed a consolidated class action complaint asserting claims under Section 10(b) of the Securities Exchange Act ("Exchange Act"), Rule 10b-5 promulgated thereunder and control person liability under Section 20(a) of the Exchange Act against numerous defendants.[2] The consolidated complaint also

---

1. Comcast merged with AT & T Broadband on December 19, 2001. (PTAC ¶ 112.)

2. The defendants named in the PTAC are Mark McEachen, George Bell and John C. Malone (the "At Home defendants"), AT & T Corporation, C. Michael Armstrong, John C. Petrillo, Daniel H. Somers, Mohan Gyani, Frank Ianna, Charles H. Noski, Raymond Liguori and Hossein Eslambolchi (the "AT & T defendants"), Kleiner Perkins Caufield & Byers, L. John Doerr, William R. Hearst, III and Thomas A. Jermoluk (the "Kleiner Perkins defendants"), Comcast Cable Communications, Inc. and Brian L. Roberts (the "Comcast defendants"), Cox Communications, Inc. and David M. Woodrow (the "Cox (Cont'd)

asserted claims of common law fraud and breaches of fiduciary duties, which were dismissed in September 2003 as preempted by the Securities Litigation Uniform Standards Act of 1998, 15 U.S.C. § 78bb(f)(1). The same order also dismissed, as mere puffery, several statements alleged as bases for liability.

On February 24, 2004, plaintiffs filed a first amended consolidated class action complaint, which added a claim under Section 14(a) of the Exchange Act alleging misrepresentations and omissions in At Home's May 26, 2000 Proxy Statement. That claim, and certain control person claims, were dismissed by order dated August 9, 2004.

By order dated March 10, 2005, a class was certified of all persons and entities that purchased the common stock of At Home during the period March 28, 2000 through September 28, 2001.

On May 31, 2005, plaintiffs moved for leave to file a second amended consolidated complaint to comply with recently decided cases addressing the issue of loss causation, and to extend the class period back to November 9, 1999. At a conference on July 8, 2005, plaintiffs were directed to file a proposed third amended

---

(Cont'd)

defendants") and Edward S. Rogers. The individual defendants were all directors or officers, or both, of At Home and (except for Eslambolchi) are alleged to be control persons of At Home. (PTAC ¶ 16-36.)

complaint (the PTAC) setting forth their best possible allegations of loss causation.

On August 5, 2005, plaintiffs moved to file the PTAC, which asserts claims under Section 10(b) against defendants AT & T, Armstrong, McEachen, Noski, Somers and Petrillo, as well as control person claims against all defendants under Section 20(a) premised on primary violations of Section 10(b) by At Home.

Defendants move to dismiss the first amended complaint, and oppose the filing of the second and proposed third amended complaints. They argue, among other things, that AT & T's scheme was not in connection with the purchase or sale of any security, that plaintiffs have not adequately pled loss causation, and that no fraudulent acts took place during the proposed extended class period.[3]

LEGAL STANDARDS

1. Motion to Dismiss

On a motion to dismiss pursuant to Federal Rule of Civil Procedure 12(b)(6), the court's function is "not to

---

3. Plaintiffs seek to extend the class period because At Home's representations that it possessed and protected proprietary technology, and the AT & T defendants' misappropriation thereof, began before March 28, 2000. Because plaintiffs do not adequately plead a securities fraud arising from either of those claims, the issue whether extending the class period is warranted need not be addressed.

weigh the evidence that might be presented at trial but merely to determine whether the complaint itself is legally sufficient." *Goldman v. Belden*, 754 F.2d 1059, 1067 (2d Cir.1985). The court must accept the plaintiff's well-pled factual allegations as true and draw all reasonable inferences in the plaintiff's favor. *Papasan*, 478 U.S. at 283, 106 S.Ct. 2932. Thus, a complaint may be dismissed only where "it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson*, 355 U.S. 41, 45-46, 78 S.Ct. 99, 102, 2 L.Ed.2d 80 (1957). In deciding a motion to dismiss, the court may consider exhibits to the complaint, documents incorporated in the complaint by reference, and matters of which judicial notice may be taken, such as public disclosure documents that are required by law to be, and have been, filed with the SEC. *Kramer v. Time Warner, Inc.*, 937 F.2d 767, 773-74 (2d Cir.1991).

2. Section 10(b) of the Exchange Act and Rule 10b-5

The majority of claims asserted under Rule 10b-5,[4]

---

4. Rule 10b-5 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,

(Cont'd)

promulgated under Section 10(b) of the Exchange Act,[5]

(Cont'd)

> (b) To make any untrue statement of a material fact, or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5.

5. Section 10 of the Exchange Act provides, in pertinent part:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—
>
> . . .
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. § 78j.

are brought under subparagraph (b), which prohibits fraudulent misstatements or omissions. To state a claim under that provision, a plaintiff must show that the defendant "(1) made misstatements or omissions of material fact; (2) with scienter; (3) in connection with the purchase or sale of securities; (4) upon which plaintiffs relied; and (5) that plaintiffs' reliance was the proximate cause of their injury." *Lentell v. Merrill Lynch & Co., Inc.*, 396 F.3d 161, 172 (2d Cir.2005), *cert. denied*, __ U.S. __, 126 S.Ct. 421, 163 L.Ed.2d 321 (2005).

In addition, the Private Securities Litigation Reform Act of 1995 ("PSLRA") requires that a complaint alleging misleading statements or omissions under Section 10(b) "specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed." 15 U.S.C. § 78u-4(b)(1). Similarly, Federal Rule of Civil Procedure 9(b)[6] requires that a complaint alleging fraud: "(1) specify the statements that the plaintiff contends were fraudulent, (2) identify the speaker, (3) state where and when the statements were made, and (4) explain why the statements were fraudulent." *Mills v. Polar Molecular Corp.*, 12 F.3d 1170, 1175 (2d Cir.1993).

6. Rule 9(b) provides that "In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person may be averred generally." Fed.R.Civ.P. 9(b).

Though often conflated with subparagraph (b), the more general provisions of subparagraphs (a) and (c) of Rule 10b-5 do not require a misstatement or omission. To make out a claim under those provisions, plaintiffs must allege that "(1) they were injured; (2) in connection with the purchase or sale of securities; (3) by relying on a market for securities; (4) controlled or artificially affected by defendant's deceptive or manipulative conduct; and (5) the defendants engaged in the manipulative conduct with scienter." *In re Initial Public Offering Sec. Litig.*, 241 F.Supp.2d 281, 385 (S.D.N.Y.2003).

Loss Causation

All private plaintiffs asserting securities fraud claims under Section 10(b) or Rule 10b-5 "must prove that the defendant's fraud caused an economic loss." *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336, 125 S.Ct. 1627, 1629, 161 L.Ed.2d 577 (2005). The common law loss causation requirement was codified in the PSLRA: "In any private action arising under this chapter, the plaintiff shall have the burden of proving that the act or omission of the defendant alleged to violate this chapter caused the loss for which the plaintiff seeks to recover damages." 15 U.S.C. § 78u-4(b)(4).

The causation element of Rule 10b-5 has two separate elements: "a plaintiff must allege both transaction causation, *i.e.*, that *but for* the fraudulent statement or omission, the plaintiff would not have entered into the transaction; and loss causation, *i.e.*, that

the subject of the fraudulent statement or omission was the cause of the actual loss suffered." *Suez Equity Investors, L.P. v. Toronto-Dominion Bank*, 250 F.3d 87, 95 (2d Cir.2001).

Plaintiffs must show that the defendants' fraud caused their losses because the securities statutes make private securities fraud actions available, "not to provide investors with broad insurance against market losses, but to protect them against those economic losses that misrepresentations actually cause." *Dura*, 125 S.Ct. at 1633; *cf. Castellano v. Young & Rubicam, Inc.*, 257 F.3d 171, 186 (2d Cir.2001) ("The loss causation requirement is intended to 'fix a legal limit on a person's responsibility, even for wrongful acts.' "), quoting *First Nationwide Bank v. Gelt Funding Corp.*, 27 F.3d 763, 769 (2d Cir.1994).

In *Dura*, the Supreme Court stated that a plaintiff who has suffered an economic loss must plead "some indication of the loss and the causal connection that the plaintiff has in mind." 125 S.Ct. at 1634. Allegations that the plaintiff purchased shares at an artificially inflated price do not, without more, plead loss causation. *Id.*[7]

---

7. Plaintiffs continue to rely on my September 17, 2003 opinion, which sustained their loss causation allegations on an inflated purchase price theory:

> that because of the defendants' failure to disclose their planned misappropriation of At Home's valuable proprietary technology, plaintiffs paid more

(Cont'd)

Appendix B

The Court of Appeals explained in *Lentell*, that to establish loss causation:

(Cont'd)

> than the fair value of At Home stock when they purchased it. On that theory, the loss is that increment of the market price representing the market's ignorance of the undisclosed facts, and the loss was caused by purchase of the stock at the market price.

Leykin v. AT & T Corp., No. 02 Civ. 1765(LLS) (S.D.N.Y. Sept. 17, 2003), at *2; (Pl. Reply at 4.) However, that opinion predated *Dura*, which states:

> [T]he logical link between the inflated share purchase price and any later economic loss is not invariably strong. Shares are normally purchased with an eye toward a later sale. But if, say, the purchaser sells the shares quickly before the relevant truth begins to leak out, the misrepresentation will not have led to any loss. If the purchaser sells later after the truth makes its way into the market place, an initially inflated purchase price *might* mean a later loss. But that is far from inevitably so. When the purchaser subsequently resells such shares, even at a lower price, that lower price may reflect, not the earlier misrepresentation, but changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events, which taken separately or together account for some or all of that lower price.

125 S. Ct. at 1631-32. Thus, that portion of my September 17, 2003 opinion is no longer good law.

Appendix B

> 'a plaintiff must allege . . . that the *subject* of the fraudulent statement or omission was 'he cause of the actual loss suffered,'*Suez Equity Investors, L.P. v. Toronto-Dominion Bank*, 250 F.3d [at 95], *i.e.*, that the misstatement or omission concealed something from the market that, when disclosed, negatively affected the value of the security. Otherwise, the loss in question was not foreseeable.

396 F.3d at 173 (emphasis in *Lentell*).

"Loss causation" in this setting is concerned less with the misrepresentation which fooled the victim into the transaction, and more with whether it was the concealed or misrepresented fact which caused the harm. "A foreseeable injury at common law is one proximately caused by the defendant's fault, but it cannot ordinarily be said that a drop in the value of a security is 'caused' by the misstatements or omissions made about it, as opposed to the underlying circumstance that is concealed or misstated." *Id.* at 173. "Put another way, a misstatement or omission is the 'proximate cause' of an investment loss if the risk that caused the loss was within the zone of risk *concealed* by the misrepresentations and omissions alleged by a disappointed investor." *Id.* (emphasis in original).

Thus, the first step in analyzing whether a complaint alleging securities fraud adequately pleads loss causation is to identify the subject of the misrepresentations or omission that allegedly caused plaintiff's loss, *i.e.*, the

risk concealed by defendant's fraud. *SeeIn re Initial Public Offering Sec. Litig.*, 399 F.Supp.2d 298, 307 (S.D.N.Y.2005) ("It is vital to understand the nature of the risks that plaintiffs in the instant action allege were concealed.").

The second step is to determine whether the complaint alleges that the concealed risk led to plaintiff's loss. "If that relationship is sufficiently direct, loss causation is established, but if the connection is attenuated, or if the plaintiff fails to demonstrate a causal connection between the content of the alleged misstatements or omissions and the harm actually suffered, a fraud claim will not lie." *Lentell*, 396 F.3d at 174 (internal quotations and citations omitted).

A concealed risk can lead to a decline in stock price either because a corrective disclosure reveals the falsity of the misrepresentations or omissions, or because the risk which was concealed materializes and causes the price decline. *SeeIn re Initial Public Offering Sec. Litig.*, 399 F.Supp.2d at 307 ("Where the alleged misstatement conceals a condition or event which then occurs and causes the plaintiff's loss, it is the materialization of the undisclosed condition or event that causes the loss. By contrast, where the alleged misstatement is an intentionally false opinion, the market will not respond to the truth until the falsity is revealed—*i.e.*, a corrective disclosure."); *In re Parmalat Sec. Litig.*, 375 F.Supp.2d 278, 305-307 (S.D.N.Y.2005) (loss causation can be pled by alleging either a corrective disclosure or the materialization of a concealed risk).

Appendix B

DISCUSSION

Six sets of allegedly fraudulent acts can be distilled from the PTAC: (1) the AT & T defendants' scheme to misappropriate At Home's proprietary technology and otherwise impede At Home's business, (2) At Home's misrepresentations that it possessed and protected valuable proprietary technology and its nondisclosure of AT & T's misappropriation, (3) At Home's false financial statements and exaggerated subscriber growth projections, (4) defendant McEachen's misrepresentations regarding At Home's performance, (5) fraudulent acts and omissions related to the March 2000 agreements, and (6) misrepresentations concealing Cox and Comcast's intentions to stop doing business with At Home.

1. The AT & T Defendants' Scheme

Plaintiffs claim that the AT & T defendants violated Section 10(b) and Rule 10b-5(a) and (c) by engaging in a fraudulent scheme to misappropriate At Home's technology, diminish its profits and impair its ability to raise capital. According to the PTAC, the scheme was carried out in the following ways:

- AT & T announced the Open Access program, which would allow customers to choose Internet Service Providers other than At Home. AT & T then used tests to prepare for Open Access as a pretext to take At Home's proprietary technology. (PTAC ¶ ¶ 59(f), (k), (t), 60.)

- AT & T appointed defendant Eslambolchi and others to At Home's management to pressure its engineers into divulging more of At Home's proprietary technology, which created a 'fear set' among At Home's employees, diminished their productivity and caused some to leave the company. *Id.* at ¶ ¶ 59(k), 81, 83(c), 94.

- AT & T forced At Home to spend $45 million over budget on computer equipment. *Id.* at ¶ 91(b).

- AT & T prevented At Home from charging AT & T subscribers for certain licenses, thereby diminishing At Home's revenues. *Id.* at ¶ 91(d).

- AT & T prevented At Home from forming a beneficial partnership or obtaining advantageous financing, forcing At Home to enter the Promethean Financing that led to its financial collapse. *Id.* at ¶¶ 100, 103.

The AT & T defendants argue that the alleged scheme was not "in connection with the purchase or sale of any security" as both Section 10(b) and Rule 10b-5 require. 15 U.S.C. § 78j(b); 17 C.F.R. § 240.10b-5. Plaintiffs respond that "At Home's proprietary technology was the key to the value of its stock and the undisclosed scheme clearly related to (and destroyed) the investment value of and price of At Home Stock." (Pl. Mem. Supp. Mot. Leave to File a Third Am. Compl. ("Pl.Mem.") at 22-23.)

Appendix B

Not all conduct that negatively affects a company's stock price is actionable as a federal securities fraud. The scheme to defraud must coincide with the sale of securities. *SEC v. Zandford*, 535 U.S. 813, 822, 122 S.Ct. 1899, 1904, 153 L.Ed.2d 1 (2002). In other words, the fraud itself must be "integral to the purchase and sale of the securities in question." *Pross v. Katz*, 784 F.2d 455, 459 (2d Cir.1986), quoted in *Dabit v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 395 F.3d 25, 37 (2d Cir.2005), *rev'd on other grounds*, __ U.S. __, 126 S.Ct. 1503, 164 L.Ed.2d 179 (2006). Conduct that is merely incidental or tangentially related to the sale of securities will not meet the "in connection with" requirement. *Ling v. Deutsche Bank, AG*, No. 04 Civ. 4566(HB), 2005 WL 1244689, at *6, 2005 U.S. Dist. LEXIS 9998, at *14 (S.D.N.Y. May 26, 2005).

Indeed, "courts repeatedly have found that allegations constituting nothing more than assertions of general mismanagement, or nondisclosures of mismanagement, cannot support claims under § 10(b) of the Exchange Act". *In re Donna Karan Int'l, Inc.*, No. 97 Civ.2011(CBA), 1998 WL 637547, at *9 (E.D.N.Y. Aug. 14, 1998); *cf. Suez Equity*, 250 F.3d at 99 ("Post-stock-purchase corporate mismanagement or breach of fiduciary duty may be just as reprehensible as a misleading statement regarding the value of a security to be sold, but the former is not proscribed by § 10(b), while the latter is actionable."); *Arduini/Messina P'ship v. Nat'l Med. Fin. Serv. Corp.*, 74 F.Supp.2d 352, 362 (S.D.N.Y.1999) (allegations of corporate mismanagement and breach of fiduciary duties might support a derivative

claim but cannot provide the basis for a securities fraud claim) (collecting cases).

In *Mutual Shares Corp. v. Genesco, Inc.*, 384 F.2d 540 (2d Cir.1967), the Court of Appeals dismissed a claim similar to the scheme alleged here. Minority shareholders claimed, among other things, that the majority shareholders ran the company in their own interests rather than the company's, by diverting company assets to themselves. *Id.* at 542. The court held that those allegations "are primarily corporate abuse and diversion, claims cognizable under state law but not under the [Exchange] Act." *Id.* at 546. As in *Mutual Shares*, the scheme alleged here involved corporate abuse, misconduct and diversion of assets, but no transactions in the relevant securities.[8] Its success

8. The *Mutual Shares* court sustained a separate claim that the majority stockholders manipulated the market price of the stock by reducing dividends in order to force minority stockholders to sell at depressed values. 384 F.2d at 547. That scheme involved market manipulation and is therefore different from the scheme alleged here. As the Supreme Court has explained, manipulation is:

> 'virtually a term of art when used in connection with securities markets.' *Ernst & Ernst [v. Hochfelder*, 425 U.S. 185, 199, 96 S.Ct. 1375, 1384, 47 L.Ed.2d 668 (1976)]. The term refers generally to practices, such as wash sales, matched orders, or rigged prices, that are intended to mislead investors by artificially affecting market activity.

Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 476, 97 S.Ct. 1292, 1302, 51 L.Ed.2d 480 (1977). Plaintiffs do not allege that defendants affected market activity in At Home stock in such a way.

depended on the misappropriation of At Home's proprietary technology, without regard to any transactions in At Home stock.

The PTAC does allege that in March 2000 AT & T increased its control over At Home by acquiring At Home shares from Cox and Comcast in exchange for AT & T shares. However, an otherwise legitimate stock transaction that is antecedent, but not integral, to the alleged fraud does not meet the "in connection with" requirement. *See Zandford*, 535 U.S. at 820, 122 S.Ct. 1899 (neither an otherwise legitimate securities transaction that is an independent event from the alleged fraud, or is merely followed by the theft of the proceeds of the transaction, supports a claim under Section 10(b)). Indeed, the defendants in *Mutual Shares*, like AT & T here, acquired a controlling position in the issuer before carrying out their scheme, 384 F.2d at 542, but the Court of Appeals nevertheless dismissed plaintiffs' claim based on the subsequent diversion of assets from the issuer. *Id.* at 546.

The cases upon which plaintiffs rely do not support the imposition of liability under Section 10(b) for the AT & T defendants' scheme. In those cases, defendants either made materially false or misleading statements upon which investors relied in purchasing or selling securities,[9] or actually traded in securities as part of the

9. *See Semerenko v. Cendant Corp.*, 223 F.3d 165 (3d Cir.2000); *In re Ames Dep't Stores, Inc. Stock Litig.*, 991 F.2d 953 (2d Cir.1993); *SEC v. Rana Research*, 8 F.3d 1358 (9th (Cont'd)

fraud.[10] Here, the alleged scheme did not involve the trading of At Home shares and, as discussed below, the alleged misrepresentations and omissions themselves could not have caused a drop in At Home's stock price.

In sum, plaintiffs' claims based on the AT & T defendants' scheme itself are dismissed as representing charges of corporate mismanagement and abuse rather than of securities fraud.[11]

(Cont'd)
Cir.1993); *Int'l Monetary Exchange v. First Data Corp.*, 63 F.Supp.2d 1261, 1265 (D.Colo.1999); *In re Leslie Fay Cos. Sec. Litig.*, 871 F.Supp. 686, 697 (S.D.N.Y.1995).

10. *See Zandford*, 535 U.S. at 815, 122 S.Ct. 1899 (broker sold customer's securities without authorization and embezzled the proceeds); *Superintendent of Ins. of the State of N.Y. v. Bankers Life and Cas. Co.*, 404 U.S. 6, 7-8, 92 S.Ct. 165, 166-67, 30 L.Ed.2d 128 (1971) (defendants purchased stock with company assets); *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 181, 84 S.Ct. 275, 277, 11 L.Ed.2d 237 (1963) (defendant recommended securities for long term investment to raise the market price and increase his own profits on sales of the securities); *Press v. Chem. Inv. Servs. Corp.*, 166 F.3d 529 (2d Cir.1999) (seller of Treasury bond failed to disclose that it would withhold interest and take a commission from the proceeds); *SEC v. Santos*, 355 F.Supp.2d 917 (N.D.Ill.2003) (bribery scheme involved investing in particular securities).

11. Claims were brought in California State court by At Home bondholders alleging that "AT & T breached fiduciary duties it owed At Home including by misappropriating At Home's proprietary information and trade secrets to build an AT & T high-speed Internet access Network to replace the At Home Network." (PTAC ¶ ¶ 55, 59(e).) AT & T agreed to settle the claims for $400 million. (Pl.'s counsel's June 3, 2005 and July 8, 2005 letters to Court.)

2. At Home's Misrepresentations Regarding its Proprietary Technology

At Home repeatedly stated in its public filings that:

> We regard our intellectual property, including our patents, copyrights, trademarks, trade secrets, and similar intellectual property as critical to our success. We rely upon patents, trademark and copyright law, trade secret protection and confidentiality or license agreements to protect our proprietary rights. Effective protection of intellectual property may not be available in every country in which our products and services are available. We cannot guarantee that the steps we have taken to protect our proprietary rights will be adequate.

At Home's Form S-3 (filed November 16, 1999) at 10, Prichard Sept. 1, 2005 Decl. Ex. 3. Plaintiffs claim that statement, and others like it,[12] were rendered misleading

12. The same language was reprinted in At Home's Form S-3/A (filed December 14, 1999) at 10, Prichard Sept. 1, 2005 Decl. Ex. 4, Form S-3/A (filed January 4, 2000) at 8, Prichard Sept. 1, 2005 Decl. Ex. 5, Form 10-K (filed March 30, 2000) at 23, Prichard Sept. 1, 2005 Decl. Ex. 6, and Form 10-K/A (filed April 28, 2000) at 25, Prichard Sept. 1, 2005 Decl. Ex. 7. *See also* At Home's Form 10-K (filed March 30, 2000), quoted at PTAC ¶ 65(a) ("We regard our technology as proprietary and we attempt to protect it under copyrights, trademarks, trade secret laws, restrictions (Cont'd)

by AT & T's misappropriation of At Home's proprietary technology, that the failure to disclose the taking was a material omission, and that those misrepresentations and omissions artificially inflated the price of At Home stock. Defendants argue that plaintiffs do not, and cannot, show that such misstatements and omissions caused At Home's stock price to fall.

Such a showing might be made if there were facts indicating that the market had learned of the AT & T defendants' intentions during the class period, or that the AT & T defendants had gained access to, copied and used At Home's proprietary technology to compete with At Home. No such facts are alleged.

No Corrective Disclosure

Despite numerous assertions that "subsidiary parts or risks" of the AT & T defendants' scheme were disclosed (PTAC ¶ 118), the PTAC does not allege facts

(Cont'd)
on disclosure and transferring title and other methods, and we have been issued patents with respect to certain aspects of our searching and indexing technology."); At Home's Form 10-K/A (filed April 28, 2000), quoted at PTAC ¶ 65(a) (same); At Home's Form 10-K (filed April 2, 2001) at 13, quoted at PTAC ¶ 96 (same and adding: "We also generally enter into confidentiality or license agreements with our employees and consultants, and generally control access to and distribution of our documentation and other proprietary information. Despite these precautions, it may be possible for a third party to copy or otherwise obtain and use our services or technology without authorization, or to develop similar technology independently.").

showing that, during the class period, the market became aware of the AT & T defendants' misappropriation of At Home's proprietary technology. On the contrary, plaintiffs acknowledge that the AT & T defendants' taking did not become public knowledge during the class period. *Id.* at ¶ 59(t) ("Pursuant to the undisclosed scheme, AT & T took a number of steps which enabled AT & T to copy At Home's technology. Some of their steps were disclosed to the public albeit the scheme, the takings, and the purpose of each step to enable AT & T to take At Home's technology were never disclosed."). Thus, the PTAC does not allege that a corrective disclosure caused At Home's stock price to decline. *See Lentell*, 396 F.3d at 175 n. 4 ("These allegations do not amount to a corrective disclosure, however, because they do not reveal to the market the falsity of the prior recommendations. . . . Merrill's concealed opinions regarding 24/7 Media and Interliant stock could not have caused a decrease in the value of those companies before the concealment was made public."); *In re WorldCom Inc. Sec. Litig.*, No. 02 Civ. 3288(DLC), 2005 WL 375314, at *6 (S.D.N.Y. Feb. 17, 2005) ("A concealed fact cannot cause a decrease in the value of a stock before the concealment is made public.").

No Materialization of the Concealed Risk

According to the PTAC, the AT & T defendants began copying At Home's proprietary technology by August or September 1999 (PTAC ¶ 59(d)), began designing their own network by October 1999, *id.* at ¶ 59(i), and had finished taking all of At Home's

proprietary technology by August 28, 2001, *id.* at ¶ 110(b). However, "AT & T's secret conversion of At Home's proprietary technology did not diminish the usefulness and general potential of such technology." *Id.* at ¶ 6.

It was not until December 2001 that AT & T's own network became operational and began servicing At Home's former customers. *Id.* at ¶ 111. That was more than a month after At Home had filed for bankruptcy, its stock had lost nearly all of its value, and, most importantly, the class period had ended.

Because the PTAC does not allege that, during the class period, At Home faced competition from its stolen technology, or that At Home's use of the technology was impaired by AT & T's misappropriation, it makes no showing that the concealed risk materialized so as to cause At Home's stock price to fall.

3. At Home's Financial Statements and Subscriber Projections

The PTAC alleges that, beginning with At Home's 10-Q filed on November 14, 2000, and continuing through 2001, At Home:

- understated accounts payable by as much as $20 million,

- overstated total stockholders' equity by as much as $100 million,

- overstated the value of its assets by as much as $80 million,

- inflated its projected number of subscribers, upon which its estimated revenues and financial performance were based,

- concealed the fact that up to $40 million in accounts payable were withheld from At Home by Cox and Comcast in 2001, and

- concealed the fact that At Home's revenues were reduced by AT & T's refusal to allow At Home to charge AT & T customers certain network usage fees. (PTAC ¶ ¶ 69, 91-92.)

Defendants argue that those claims must also be rejected for failure to plead loss causation.

No Corrective Disclosure

Plaintiffs point to At Home's Form S-3 Registration Statement filed on July 23, 2001, which stated "We will need to raise additional funds before the end of 2001 to support our business operations" and warned that failure to do so could "have a material adverse impact on our operations and liquidity" (PTAC ¶ ¶ 106, 118(J)), At Home's Form 10-K/A filed August 20, 2001 which announced "substantial doubt about our ability to continue as a going concern" and that At Home "cannot guarantee that we will be able to obtain additional funding on acceptable terms, if at all" (PTAC ¶ 107), and

the announcements of the Promethean Financing and At Home's bankruptcy filing. (Pl. Mem. Supp. Leave to Amend and Opp. Def. Mot. Dismiss ("Pl.Reply") at 93-94.)

As dire as those statements were, and as grave as the Promethean Financing and bankruptcy filing turned out to be, nothing in those statements disclosed that the alleged misrepresentations had been false or misleading. They did not reveal to the market any misstatements in At Home's prior financial reports or subscriber projections. *See Lentell*, 396 F.3d at 175 n. 4; *In re Tellium, Inc. Sec. Litig.*, No. 02 Civ. 5878(FLW), 2005 WL 2090254, at *4 (D.N.J. Aug. 26, 2005) ("*Dura* itself makes clear that loss causation is not pled upon allegations of drops in stock price following an announcement of bad news that does not disclose the fraud.").

No Materialization of the Concealed Risk

In their reply brief, plaintiffs seem to argue that the risk concealed by those misrepresentations materialized when At Home experienced a liquidity crisis in July 2001, forcing it to engage in the Promethean Financing and ultimately file for bankruptcy.

Defendants respond that the first allegedly fraudulent financial report, At Home's Form 10-Q filed November 14, 2000, disclosed that At Home might not be able to obtain financing:

Appendix B

We intend to make investments in our infrastructure of approximately $250 million during 2000, including investments in our network designed to provide stability and scaleability. Of this amount, we had invested $199.6 million during the nine months ended September 30, 2000, including purchases of property, equipment and improvements, payments on capital lease obligations and payments under our backbone agreement. We believe that we have sufficient liquidity to continue to support such investments, to meet the commitments described below and to fund our operating needs for at least the next 12 months. However, it is possible that we could experience unexpected costs and expenses with respect to these or other items. Thereafter, if cash generated by operations is insufficient to satisfy our liquidity requirements, we may need to seek alternative financing, such as selling additional equity or debt securities or obtaining additional credit facilities. However, depending on market conditions, we may consider alternative financing even if our financial resources are adequate to meet presently anticipated business requirements. Financing may not be available on terms acceptable to us or at all. The sale of additional equity or convertible debt securities may result in additional dilution to our stockholders.

At Home's Form 10-Q (filed Nov. 14, 2000) at 27, Brusca Decl. Ex. 18.

Defendants also argue that the downturn in the stock market for Internet-related companies, rather than any firm-specific financial misrepresentations, caused At Home's stock to collapse. They point out that, like At Home's stock, both market-wide and industry-specific stock indices declined dramatically between March 2000 and September 28, 2001.[13] The companies tracked by BUSNICS and BUSNISE, like At Home, provide Internet content and services. PTAC ¶ 2(b), Pl. Reply at 50 n. 17. In addition, At Home's stock performance mimicked those indices remarkably closely, especially after the alleged misrepresentations first appeared in November 2000.

In *Lentell*, the court stated that:

> where (as here) substantial indicia of the risk that materialized are unambiguously apparent

13. *See* AT & T Mem. Opp. Mot. Leave to File Third Am. Compl. ("AT & T Mem.") at 8 n. 11 (from March 27, 2000 to September 28, 2001, At Home's stock price declined 99.54%, the NASDAQ Composite Index (on which At Home stock was traded) declined 69.77%, the DJINET (Dow Jones Internet Composite Index) declined 91.52%, the BUSNICS (Bloomberg U.S. Internet Connectivity Services Index) declined 99.13% and the BUSNICE (Bloomberg U.S. Internet Content Entertainment Index) declined 89.7% from March 27, 2000 to August 29, 2001, when it was suspended); Winter Sept. 2, 2005 Aff. Ex. 20-30; Prichard Sept. 1, 2005 Aff. Ex. 14-21.

> on the face of the disclosures alleged to conceal the very same risk, a plaintiff must allege (i) facts sufficient to support an inference that it was defendant's fraud-rather than other salient factors—that proximately caused plaintiff's loss; or (ii) facts sufficient to apportion the losses between the disclosed and concealed portions of the risk that ultimately destroyed an investment.

396 F.3d at 177.

As a general proposition, whether "the loss was caused by an intervening event, like a general fall in the price of Internet stocks . . . is a matter of proof at trial and not to be decided on a Rule 12(b)(6) motion to dismiss." *Emergent Capital*, 343 F.3d at 197. However,

> "when the plaintiff's loss coincides with a marketwide phenomenon causing comparable losses to other investors, the prospect that the plaintiff's loss was caused by the fraud decreases," and a plaintiff's claim fails when "it has not adequately ple[ ]d facts which, if proven, would show that its loss was caused by the alleged misstatements as opposed to intervening events."

Lentell, 396 F.3d at 174, quoting *First Nationwide Bank*, 27 F.3d at 772.

Appendix B

The only allegation in the PTAC of a causal link between the alleged misrepresentations and the liquidity crisis is: "If the true subscriber growth and prospects had been as represented, At Home would have had more financial strength and would not have had to file for bankruptcy as it did." (PTAC ¶ 92(b).) Such an assertion is too general and conclusory to support an inference that defendants' fraud proximately caused the decline in stock prices. *See In re The Warnaco Group, Inc. Sec. Litig. (II)*, 388 F.Supp.2d 307, 318 (S.D.N.Y.2005) (unsupported assertion that "Waranco's true undisclosed financial condition rendered Waranco unable to obtain waivers" from its creditors did not support an inference that defendant's fraud proximately caused plaintiff's stock market loss). The PTAC does not allege facts showing that it was the claimed concealment which caused plaintiffs' losses, rather than the the market-wide Internet stock collapse,[14]—nor any way to separate the effect of the misstatements (if there was any) from the general collapse or other causes. Thus, there is no effective pleading of a loss caused by those misrepresentations. *See Lentell*, 396 F.3d at 174, 177. The claims based on At Home's financial statements and subscriber projections must therefore be dismissed.

---

14. In fact, the PTAC elsewhere alleges that At Home's liquidity crisis was caused by the fact that AT & T obstructed At Home from accessing capital markets or aligning with a strategic partner, and the fact that Cox and Comcast refused to enter new MDAs and planned to end their relationships with At Home. (PTAC ¶ ¶ 75(e), 103.)

4. McEachen's Statements Regarding At Home's Performance

The PTAC alleges that Mr. McEachen, At Home's chief financial officer, misrepresented At Home's financial prospects. In a January 25, 2001 Bloomberg interview, he stated that "The first quarter will be by far the low-water mark for our financial performance in 2001" (PTAC ¶ 92(a)(1)) and in a June 19, 2001 investor conference call he stated that "by getting the $185 Million [from the Promethean Financing and the IRU recapture agreement] in the till, it allows us to not have to worry in the near term about financing" (PTAC ¶ 101). Those statements are dismissed as bases for liability because they are mere generalized expressions of puffery and optimism, which are not actionable under the securities laws. *See Rombach v. Chang*, 355 F.3d 164, 174 (2d Cir.2004); *In re Duane Reade Inc. Sec. Litig.*, No. 02 Civ. 6478(NRB), 2003 WL 22801416, at *4 (S.D.N.Y. Nov. 25, 2003) ("A company's statements of hope, opinion, or belief about its future performance or general market conditions are not actionable under the securities laws."), *aff'd sub nom. Nadoff v. Duane Reade, Inc.*, 107 Fed.Appx. 250, 252 (2d Cir.2004) (summary order).

Similarly non-actionable, because of their vagueness and generality, are McEachen's April 23, 2001 statement in Business Wire that "We performed very well in our core broadband operations, which now make up nearly two-thirds of our total revenue" (PTAC ¶ 97) and Mr. Bell's April 17, 2001 statement that "Our core broadband business is strong." *Id.*

5. March 2000 Agreements

The PTAC alleges several fraudulent acts related to the March 2000 agreements between At Home and its cable partners.

The claim that AT & T's acquisition of a 74% voting interest in At Home violated Section 10(b) because it allowed the AT & T defendants to further their scheme to take At Home's proprietary technology (PTAC ¶ 61(e)) must be rejected because the PTAC does not allege that that transaction was independently fraudulent and, as discussed above, the undisclosed misappropriation of At Home's proprietary technology cannot alone support a federal securities fraud claim.

In March 2000, AT & T allegedly represented that it would execute a new non-exclusive MDA covering its relationship with At Home from June 4, 2002 through June 4, 2006 as promptly as practicable.[15] (PTAC ¶¶ 59(t), 62, 119(A)(5).) That representation was allegedly fraudulent because AT & T had no intention of executing a new MDA or continuing its relationship with At Home. Although the 1996 MDA between At Home and AT & T provided that it would remain in effect through June 2002, plaintiffs claim that the failure to execute a new MDA after March 2000 caused At Home's stock price to

15. The PTAC also alleges that Cox and Comcast misrepresented their intentions to enter new MDAs with At Home in March 2000. (PTAC ¶ ¶ 62, 119(A)(5).) Those alleged misrepresentations need not be considered as bases for liability, however, because no Section 10(b) claim is asserted against them.

fall: "According to defendant Bell, this tactical, on-going failure to achieve any amended MDA concerned market analysts and participants during 2000 and reduced the price of At Home's stock during 2000." (PTAC ¶ 118(B).)

Accepting the proposition that there could be such a market perception, plaintiffs point to no fact (such as an analyst's report or investor communication) evincing that there actually was. Plaintiffs plead no fact which, if proven, would indicate that the gradual decline in At Home's stock price during all of 2000 was caused by any concern about the absence of a new MDA, rather than other causes such as the contemporaneous market-wide Internet stock collapse. As the Supreme Court stated in *Dura*,"that lower price may reflect, not the earlier misrepresentation, but changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events, which taken separately or together account for some or all of that lower price." 125 S.Ct. at 1632. Therefore, plaintiffs have " 'not adequately pled facts which, if proven, would show that its loss was caused by the alleged misstatements as opposed to intervening events.' " *Lentell*, 396 F.3d at 174, quoting *First Nationwide Bank*, 27 F.3d at 772. Nor does the PTAC suggest any theory by which a loss attributable to such a market suspicion could be quantified. *See supra* p. 246; *Lentell*, 396 F.3d at 174, 177.

6. Cox's and Comcast's Undisclosed Intentions to End their Relationships with At Home

The PTAC refers to several statements as misrepresenting the strength of At Home's relationship with Cox and Comcast. Only two such statements survive my order dated September 17, 2003. The first is Mr. McEachen's statement in the June 19, 2001 investor and analyst conference call. Responding to a question whether Cox and Comcast would revoke their business relationships with At Home, Mr. McEachen stated that " There isn't going to be one day where we wake up in a different world and all of the co-branded Subs that we have with both of these great partners are going to migrate over to somebody else. That won't happen." (PTAC ¶ 102.) That statement was allegedly false and misleading because by that time both Cox and Comcast (1) had told At Home that neither had any interest in any future relationship with At Home, (2) were seeking to obtain At Home's technology to offer broadband services themselves and (3) also on June 19, 2001, notified At Home that they were terminating certain exclusivity provisions in their 1996 MDAs with At Home effective December 4, 2001. (PTAC ¶ 102.)

However, the PTAC does not allege that Cox or Comcast stopped doing business with At Home or provided high-speed Internet services on their own during the class period. Nor did the market learn of Cox's and Comcast's intentions to do so. McEachen's June 19, 2001 statement must therefore be dismissed for failure to plead loss causation. *Lentell*, 396 F.3d at 173.

The PTAC also alleges that At Home's statement that, "our cable partners may determine in the future that they

can provide broadband services themselves, rather than offering our services" in its Form 10-K filed April 2, 2001 was false or misleading in light of Cox's and Comcast's intentions to end their relationships with At Home and to provide aspects of At Home's services themselves. (PTAC ¶ 95.) There is no allegation, however, that any of At Home's cable partners actually provided broadband services themselves during the class period. At most, there was a risk that they might do so in the future, which is the risk of which At Home warned. Thus, that statement must be dismissed as a basis for liability.

Section 20(a) Claims

"In order to establish a *prima facie* case of liability under § 20(a), a plaintiff must show: (1) a primary violation by a controlled person; (2) control of the primary violator by the defendant; and (3) 'that the controlling person was in some meaningful sense a culpable participant' in the primary violation." *Boguslavsky v. Kaplan*, 159 F.3d 715, 720 (2d Cir.1998), quoting *SEC v. First Jersey Sec. Inc.*, 101 F.3d 1450, 1472 (2d Cir.1996).

The control person claims under Section 20(a)[16] asserted against all defendants are premised on a primary

16. Section 20(a) of the Exchange Act provides:

> Every person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable, unless the controlling person

(Cont'd)

violation of Section 10(b) by At Home. (PTAC ¶¶ 130-132.) Because all claims of primary liability have been dismissed, the Section 20(a) claims must also be dismissed. *Rombach*, 355 F.3d at 177-78.

CONCLUSION

For the reasons above, (1) defendants' motions dated September 2, 2005 to dismiss the first amended complaint are granted, (2) plaintiffs' motion dated May 31, 2005 for leave to file a second amended complaint is denied and (3) plaintiffs' motion dated August 5, 2005 for leave to file a third amended complaint is denied.

The Clerk will enter judgment dismissing all the complaints in this and the consolidated actions and dismissing as moot all other pending motions, with costs and disbursements to defendants according to law.

So ordered.

Dated: New York, NY
March 23, 2006

s/ Louis L. Stanton
LOUIS L. STANTON
U.S.D.J.

(Cont'd)

acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.

15 U.S.C. § 78t(a).

APPENDIX C — MEMORANDUM ENDORSEMENT

Semen Leykin, On Behalf of Himself and All Other Persons Similarly Situated, v. AT&T Corporation, et al., 02 Civ. 1765 (LLS)

All motions to dismiss the complaint are denied, except that:

1. Mr. Armstrong's August 28, 2000 news-release statement that "[w]orking together, Excite@Home and AT&T will bring high-speed Internet services to millions of homes and businesses and seize a great growth opportunity" [Complt ¶ 70(d)] and Mr. Armstrong's and Mr. Roberts' statements on March 29, 2000 that the March 28, 2000 agreements were "really a new commitment by AT&T, Comcast, and Cox to both our broadband business and technology, as well as Excite@Home" and "I think both the company, the people, the marketplace and the customers now can feel with a great deal of certainty the commitment of AT&T, Cox and Comcast to broadband and to Excite@Home" (Complt ¶ 63) and "From the outset, we have viewed Excite@Home as an invaluable strategic partner. . . . The extension of our agreements gives us clarity and the ability to continue our aggressive deployment of Comcast@Home" and "We are pleased to extend our relationship with Excite@Home" (Complt ¶ 64) and Mr. Jenner's February 14, 2001 statement "Working together we've got it all" (Complt ¶ 93) are dismissed as bases of liability, as merely generalized expressions of confidence and optimism, constituting "puffery" which cannot mislead a reasonable investor or constitute

actionable statements under the securities laws, *see San Leandro Emerg. Med. Plan v. Philip Morris Cos., Inc.*, 75 F.3d 801, 811 (2d Cir. 1996) ; *Steinberg v. PRT Group, Inc.*, 88 F.Supp.2d 294, 301 (S.D.N.Y. 2000);

2. The THIRD and FOURTH claims are dismissed as pre-empted and barred by the Securities Litigation Uniform Standards Act, 15 U.S.C. § 78bb(f)(1) ("SLUSA") which provides:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging—
>
> > (A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security; or
> >
> > (B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

Plaintiffs' arguments that SLUSA does not apply, *e.g.*, because of the "Delaware carve-out," are unavailing. *See Zoren v. Genesis Energy, L.P.*, 195 F.Supp.2d 598 (D. Del. 2002); *Professional Management Associates v. KPMG LLP*, 335 F.3d 800, 803 (8th Cir. 2003) ("PMA

cannot avoid preemption by asserting it is only claiming damages suffered as a result of holding its stock. [citing *Zoren*] SLUSA's "in connection with" requirement [citation] is not limited to cases involving damages claimed as a result of the purchase or sale of securities. Instead, SLUSA applies to any covered class action alleging an untrue statement or omission of a material fact in connection with the purchase or sale of a covered security."); and

3. Plaintiffs have withdrawn their claims against Mr. Cinali.

Defendants' argument that plaintiffs inadequately show loss causation disregards the basic nature of the claim: that because of the defendants' failure to disclose their planned misappropriation of At Home's valuable proprietary technology, plaintiffs paid more than the fair value of At Home stock when they purchased it. On that theory, the loss is that increment of the market price representing the market's ignorance of the undisclosed facts, and the loss was caused by purchase of the stock at the market price. *See Suez Equity Investors v. Toronto-Dominion Bank*, 250 F.3d 87, 97-98 (2nd Cir. 2001) ("plaintiffs may allege transaction and loss causation by averring both that they would not have entered the transaction but for the misrepresentations and that the defendants' misrepresentations induced a disparity between the transaction price and the true 'investment quality' of the securities at the time of transaction"); *Semerenko v. Cendant Corp.*, 223 F.3d 165, 184 (3rd Cir. 2000) ("where the claimed loss involves the

purchase of a security at a price that is inflated due to an alleged misrepresentation, there is a sufficient causal nexus between the loss and the alleged misrepresentation to satisfy the loss causation requirement").

The allegations here are a far cry from overstatements of the investment value of a stock followed by its depreciation in a general market decline, as in *In re Merrill Lynch & Co., Inc. Research Reports Sec. Litig.*, 02 MDL 1484 (MP) , 2003 WL 21500293, at *9-12 (S.D.N.Y. June 30, 2003) (holding that plaintiffs failed to tie inflated investment analyst ratings to the actual financial demise of the recommended companies). The legal analysis on this point is fact-specific. *See Suez Equity Investors*, 250 F.3d at 96 ("loss causation inquiry typically examines how directly the subject of the fraudulent statement caused the loss, and whether the resulting loss was a foreseeable outcome of the fraudulent statement"). In *Merrill Lynch*, the analysts' stock recommendations would not cause the price to drop. Other factors, unrelated to the analysts, caused the price to drop. In this case, at least for pleading purposes, the undisclosed theft of the "crown jewels" made a loss inevitable.

The affirmative defense of the statute of limitations is insufficiently established on this record to justify dismissal of the FIRST and SECOND claims on that ground as a matter of law.

So ordered.

DATED: New York, New York
September 17, 2003

s/ Louis L. Stanton
LOUIS L. STANTON U. S. D. J.

APPENDIX D — MEMORANDUM ENDORSEMENT

Semen Leykin, On Behalf of Himself and All Other Persons Similarly Situated v. AT&T Corporation, et al., 02 Civ. 1765 (LLS)

Defendants' motions to dismiss Claim Five of the First Amended Consolidated Class Action Complaint are granted. There is no statement in At Home's Form 14A Proxy Statement dated May 26, 2000 which is rendered false or misleading by the omission to set forth the planned misappropriation of At Homes' valuable proprietary technology. The Proxy Statement accurately describes the proposed changes in governance, which would "grant AT&T voting control of all board actions" of At Home (as conceded in Amended Complaint ¶¶ 66, 137). Nothing in its subject matter is inaccurately described in the Proxy Statement.

Nor was it necessary for the Proxy Statement to disclose AT&T's alleged plan to misappropriate At Home's technology. Section 14(a) of the Exchange Act, 15 U.S.C. § 78n(a), and cognate Rule 14, 17 C.F.R. § 240.14, do not require the disclosure of subjective purposes of transactions accurately set forth in a proxy statement. *See Virginia Bankshares v. Sandberg*, 501 U.S. 1083, 1096 (1991) ("to recognize liability on mere disbelief or undisclosed motive without any demonstration that the proxy statement was false or misleading about its subject would authorize Section 14(a) litigation confined solely to what one skeptical court spoke of as the 'impurities' of a director's 'unclean heart'"); *Maldonado v. Flynn*, 597 F.2d 789, 796 (2d Cir.

1979) (distinguishing between nondisclosure of self-dealing on the basis of inside information, against corporation's interest, on the one hand, and mere "failure to disclose an alleged ulterior motive for a fully described corporate action" which is insufficient under Section 14 (a)) .

Dismissal of Claim Five carries with it dismissal of the related § 20(a) "control persons" claims against the individual defendants named only in connection with Claim Five.

In addition, all claims as a "control person" are dismissed as against Mr. Gyani with respect to the period before he became an At Home director in June 2000, with respect to Mr. Liguori after he ceased to be a member of the At Home board of directors in June 2000, and with respect to Mr. Noski before he became a director of At Home in February 2001.

Mr. Rogers' motion for dismissal of the Second Claim against him as a "control person" in the First Amended Consolidated Class Action Complaint is granted with respect to periods when he was not serving as a director of At Home, except for documents he signed, actions he took or statements he made outside those periods of service.

Plaintiffs have had, and used, sufficient opportunities for corrections and amendment of their pleadings. Further leave to amend is denied.

So ordered.

DATED: New York, New York
August 9, 2004

s/ Louis L. Stanton
LOUIS L. STANTON
U.S.D.J.

APPENDIX E — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT DENYING PETITION FOR REHEARING FILED JULY 9, 2007

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Catherine O'Hagan Wolfe
CLERK

Date:	7/9/07
Docket Number:	06-1583-cv
Short Title:	Leykin v. AT&T Corporation
DC Docket Number:	02-cv-1765
DC:	SDNY (NEW YORK CITY)
DC Judge:	Honorable Louis Stanton

At a stated term of the United States Court of Appeals for the Second Circuit, held at the Daniel Patrick Moynihan United States Courthouse, 500 Pearl Street, in the City of New York, on the 9th day of July two thousand seven.

Semen Leykin,

Plaintiff-Appellant,

v

AT&T Corporation,

Defendant-Appellees,

Appendix E

A petition for panel rehearing and a petition for rehearing en banc having been filed herein by the appellant Semen Leykin. Upon consideration by the panel that decided the appeal, it is Ordered that said petition for rehearing is **DENIED.**

It is further noted that the petition for rehearing en banc has been transmitted to the judges for the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

For the Court,
Catherine O'Hagan Wolfe, Clerk

By: s/ Arthur Heller
Motion Staff Attorney

APPENDIX F — STATUTES AND REGULATIONS INVOLVED

The relevant statutory and regulatory provisions, Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (the "Exchange Act"), Section 21D(b)(4) of the Exchange Act, 15 U.S.C. § 78u-4(b)(4), SEC Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5 (2004), and SEC Regulation S-K, Item 404(a), 17 C.F.R. § 229.404(a) (1988) are set forth below.

Section 10(b) of the Securities Exchange Act, 15 U.S.C. § 78j(b), provides as follows:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange–
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement (as defined in section 206B of the Gramm-Leach-Bliley Act), any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Appendix F

Section 21D(b)(4) of the Securities Exchange Act, 15 U.S.C. § 78u-4(b)(4), provides as follows:

> In any private action arising under this chapter, the plaintiff shall have the burden of proving that the act or omission of the defendant alleged to violate this chapter caused the loss for which the plaintiff seeks to recover damages.

SEC Rule 10b-5, 17 C.F.R. § 240.10b-5 provides as follows:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Appendix F

SEC Regulation S-K, Item 404(a), 17 C.F.R. § 229.404(a), at all times pertinent hereto provided in relevant part as follows:

> *Transactions With Management and Others.* Describe briefly any transaction, or series of similar transactions, since the beginning of the registrant's last fiscal year, or any currently proposed transaction, or series of similar transactions, to which the registrant or any of its subsidiaries was or is to be a party, in which the amount involved exceeds $60,000, and in which any of the following persons had, or will have, a direct or indirect material interest . . . (1) Any director or executive officer of the registrant; (2) Any nominee for election as a director; (3) Any security holder who is known to the registrant to own more than five percent of any class of the registrant's voting securities . . . .

FILED
NOV 13 2007
OFFICE OF THE CLERK
SUPREME COURT, U.S.

No. 07-484

IN THE

Supreme Court of the United States

SEMEN LEYKIN, *et al.*,

Petitioners,

v.

AT&T CORPORATION, *et al.*,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

RESPONDENTS' BRIEF IN OPPOSITION

WAYNE WATTS
SENIOR EXECUTIVE VICE PRESIDENT AND GENERAL COUNSEL
AT&T CORP.
175 E. Houston Street
San Antonio, TX 78205
(210) 351-3300

DAVID W. CARPENTER*
STEPHEN C. CARLSON
RACHEL B. NIEWOEHNER
DANIEL S. RYAN
SIDLEY AUSTIN LLP
One South Dearborn Street
Chicago, IL 60603
(312) 853-7000

EDWARD R. BARILLARI
SENIOR VICE PRESIDENT AND ASSISTANT GENERAL COUNSEL
AT&T CORP.
One AT&T Way
Bedminster, NJ 07921
(908) 532-1885

Counsel for AT&T Respondents

November 13, 2007 * Counsel of Record

[Additional Counsel Listed on Inside Cover]

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20002

JONATHAN E. RICH
PROSKAUER ROSE LLP
2049 Century Park East
Suite 3200
Los Angeles, CA 90067
(310) 284-5644

Counsel for Respondent Mark McEachen

QUESTIONS RESTATED

Whether the Second Circuit correctly held that petitioners had not stated a claim for securities fraud under Section 10(b) of the Securities Exchange Act and Rule 10b-5 where (1) the alleged misrepresentations and omissions of material facts concededly did not cause a reduction in the stock price or losses to petitioners during the class period and (2) the remaining allegations were acts of corporate mismanagement and breaches of fiduciary duties that are not actionable as securities fraud under the Securities Exchange Act of 1934 and that were independent of any securities transactions?

PARTIES TO THE PROCEEDING

The Petition (p. iii) lists the individuals and corporations that are now parties to this proceeding.

Pursuant to Rule 29.6, respondent AT&T Corp. states that it is a wholly-owned subsidiary of AT&T Inc., a publicly traded company.

TABLE OF CONTENTS

	Page
QUESTIONS RESTATED	i
PARTIES TO THE PROCEEDING	ii
TABLE OF AUTHORITIES	iv
BRIEF IN OPPOSITION	1
COUNTERSTATEMENT OF THE CASE	3
REASONS FOR DENYING THE PETITION	8
I. DISMISSAL OF THE "SCHEME" CLAIMS WAS A CORRECT APPLICATION OF SETTLED PRINCIPLES	8
II. THE APPLICATION OF *DURA* PRESENTS NO ISSUE FOR REVIEW	15
CONCLUSION	19

TABLE OF AUTHORITIES

CASES Page

Affiliated Ute Citizens of Utah v. United States, 406 U.S. 128 (1972) 13
In re Charter Commc'ns, Inc. Sec. Litig., 443 F.3d 987 (8th Cir. 2006), *cert. granted sub nom. Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 127 S. Ct. 1873 (2007) (No. 06-43) 11
Dura Pharms., Inc. v. Broudo, 544 U.S. 336 (2005) 2, 10, 15-18
Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976) 18
Lentell v. Merrill Lynch & Co., Inc., 396 F.3d 161 (2d Cir.), *cert. denied*, 546 U.S. 935 (2005) 16
Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit, 547 U.S. 71 (2006) 13
Mutual Shares Corp. v. Genesco, Inc., 384 F.2d 540 (2d Cir. 1967) 2, 9-10
Ray v. Citigroup Global Mkts., Inc., 482 F.3d 991 (7th Cir. 2007) 16
Regents of Univ. of Calif. v. Credit Suisse First Boston, Inc., 482 F.3d 372 (5th Cir. 2007), *petition for cert. filed*, 75 U.S.L.W. 3557 (U.S. Apr. 5, 2007) (No. 06-1341) 11-13
Robbins v. Koger Props., Inc., 116 F.3d 1441 (11th Cir. 1997) 16
Santa Fe Indus., Inc. v. Green, 430 U.S. 462 (1977) 2, 9-10, 15
SEC v. Zandford, 535 U.S. 813 (2002) .. 9, 13-14
Simpson v. AOL Time Warner Inc., 452 F.3d 1040 (9th Cir. 2006), *petition for cert. for filed*, 75 U.S.L.W. 3236 (U.S. Oct. 19, 2006) (No. 06-560) 11-13

TABLE OF AUTHORITIES – continued

Page

Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc., 127 S. Ct. 1873 (No. 06-43) 2, 11-13
Superintendent of Ins. of State of N.Y. v. Bankers Life & Cas. Co., 404 U.S. 6 (1971) 9, 13
Teachers' Ret. Sys. of La. v. Hunter, 477 F.3d 162 (4th Cir. 2007) 16
United States v. *O'Hagan*, 521 U.S. 642 (1997) 9, 13

STATUTES AND REGULATIONS

15 U.S.C. § 78j(b) ..... *passim*
§ 78n(a) 1, 7
§ 78t(a) 4, 12
§ 78u-4(b)(4) 16
17 C.F.R. § 229.404(a) 14-15
§ 240.10b-5 ..... 2, 6, 11-12

RULE

Second Circuit's R. 32.1(b) 15

IN THE

Supreme Court of the United States

No. 07-484

SEMEN LEYKIN, *et al.*,

Petitioners,

v.

AT&T CORPORATION, *et al.*,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

RESPONDENTS' BRIEF IN OPPOSITION

Petitioners are here seeking review of an unpublished summary order in which the Second Circuit upheld the dismissal of a private securities fraud complaint for failure to state a claim upon which relief can be granted under Sections 10(b) and 14(a) of the Securities Exchange Act of 1934.

This Second Circuit order does not present the questions, or the conflicts with other decisions, that are alleged in the Petition. Rather, as petitioners correctly stated below, the claims that they have raised are "*sui generis*," and the Second Circuit's summary order is a correct application of well-settled principles to quite unique factual allegations.

First, petitioners' primary claim was barred by their inability to allege loss causation under the standards of *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005), and of each federal court of appeals to have addressed this issue. Petitioners alleged that respondents made fraudulent misrepresentations and omissions that inflated the stock price of At Home Corporation. However, the allegations of the complaint also established that petitioners' stock had lost its value for other independent reasons long *before* the alleged concealed facts were revealed to the market.

Second, petitioners' remaining allegations did not raise any novel issues about the scope of "scheme" liability under Section 10(b). To the contrary, those allegations consisted of claims of corporate mismanagement and abuse that are actionable only as state law breach of fiduciary duty claims and that also were independent of any securities transactions. *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 478-79 (1977); *Mutual Shares Corp. v. Genesco, Inc.*, 384 F.2d 540, 545-546 (2d Cir. 1967).

In this regard, this case does not raise, and the Second Circuit did not address, the question presented in *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, No. 06-43: whether private 10b-5 actions can be maintained against third parties who make no misrepresentations but who allegedly engaged in transactions with a stock issuer that had the purpose and effect of misleading the public about the financial condition of the issuer. There is thus no reason to hold this case for *Stoneridge*.

COUNTERSTATEMENT OF THE CASE

1. At Home Corporation ("At Home") was a provider of Internet services. At the beginning of the period at issue in this case, over half of At Home's revenues were from Internet content services offered in competition with entities like Yahoo. The rest of its revenues were from wholesale Internet access services provided to AT&T, Cox, Comcast, and other operators of cable television systems.

AT&T Corp. was a major shareholder with representation on At Home's board throughout the relevant period. In addition, AT&T acquired full voting control of At Home in August 2000 as a result of stock purchases (via a put agreement) with Cox and Comcast and other transactions announced in March 2000.

Throughout its existence, At Home had quarterly losses of many hundreds of millions of dollars and disclosed the substantial financial and business risks that it faced in its SEC filings and other public statements. Nonetheless, At Home enjoyed a stock price of over $90 per share at the height of the Internet "bubble," and its stock price was $49 per share at the beginning of the class period. Following the bursting of the Internet bubble in March 2000, At Home's stock price fell in virtual lockstep with Internet stock indices (App. 37a & n.13), and it was pennies per share when At Home declared bankruptcy on September 28, 2001. At Home ceased operations shortly thereafter.

2. This action was brought on behalf of all persons who had purchased the stock of At Home between November 9, 1999 and September 28, 2001 ("the class period"). The defendants now consist of AT&T Corp.

and various of its officers who were directors or officers of At Home (collectively referred to as "AT&T respondents") as well as a former At Home officer, Mark McEachen.[1] The issue in this case is the legal sufficiency of Plaintiffs' Proposed Third Amended Complaint ("PTAC").

In the PTAC, petitioners essentially made two sets of allegations. First, they alleged a traditional securities fraud action. They contended At Home had made misrepresentations and omissions that had artificially inflated the price of At Home's stock throughout the class period (and that AT&T and the individual defendants were liable for this conduct as "control persons" under § 20(a) of the Securities Exchange Act and/or as signatories of SEC documents).

In particular, petitioners' primary allegation was that At Home had stated that it was protecting the intellectual property that was critical to its success, but that these statements were false and misleading because At Home knew that AT&T was copying and misappropriating At Home's intellectual property. Petitioners also alleged that At Home's financial statements had not fully disclosed the precariousness of its financial condition – a claim that petitioners have dropped in this Court. The District Court dismissed both of these allegations for failure to plead "loss causation" within the meaning of *Dura*, and the Second Circuit summarily affirmed this holding.

---

[1] In the lower courts, petitioners also pursued claims against Comcast, Cox, Kleiner Perkins Caufield & Byers, and various individual defendants. Petitioners dropped their claims against these other parties in this Court.

Second, petitioners made a series of allegations to the effect that AT&T had abused its position as a major and, later, controlling shareholder of At Home and committed a number of acts that weakened At Home financially, pressured it into allowing AT&T to access and copy intellectual property, and caused or contributed to At Home's bankruptcy. These included announcing "open access" on December 6, 1999, requiring At Home to prepare its network to provide this access, agreeing to acquire voting control of At Home in March 2000, requiring At Home to increase its capital expenditures, interfering with At Home's efforts to obtain financing, and other similar conduct. App. 9a-12a; Pet. at 8-14. Petitioners alleged that all this conduct was part of a single nefarious "scheme" that was designed to enable AT&T first to maintain At Home in a weakened state while AT&T copied its technology and then to end its life and begin using At Home's technology to provide wholesale Internet access service itself.

All petitioners' "scheme" allegations were expressly derived from a parallel state court action in which a trustee for At Home sought to recover (on behalf of shareholders and bondholders) damages for alleged breaches by AT&T of its fiduciary duties as At Home's controlling shareholder. *See* PTAC, ¶¶ 55, 58, 59(e)-(q), & 110(b) (referring to this action by name and repeating allegations from it). This state court suit is the action that AT&T settled for $400 million (out of a claimed $3 billion). *See* Pet. at 13.

Petitioners alleged that the nondisclosure of AT&T's purported scheme to harm At Home had artificially inflated the price of At Home's stock throughout the class period. At the same time, although this action was brought on behalf of persons

who purchased stock at these purportedly inflated prices during the class period, petitioners incongruously alleged that AT&T's abusive conduct had simultaneously *deflated* At Home's stock price. In particular, they claimed that AT&T's conduct artificially lowered the price of At Home's stock both at the virtual inception of the class period (the December 6, 1999 open access announcement) and at a date early in the class period (the March 2000 announcement of the transaction in which AT&T would acquire voting control). Petitioners maintained that their allegations that acts of mismanagement artificially reduced At Home's stock price rendered their securities law claims "*sui generis*" and somehow supported the fraud claims that they brought as *purchasers* of securities. Appellants' Corrected Reply Brief, p. 39 (Filed in Second Circuit Dec. 5, 2006).

3. The District Court held that the PTAC did not state a claim for securities fraud and the Second Circuit summarily affirmed this ruling.

First, the District Court assumed, *arguendo,* that petitioners had sufficiently pled misrepresentations and omissions within the meaning of Rule 10b-5 by alleging that At Home had stated that it was protecting its intellectual property without disclosing AT&T's alleged misappropriation of it. But the District Court held that these allegations were insufficient to state a securities fraud claim because petitioners had not (and could not) allege that their losses had been caused by these misrepresentations and omissions, rather than by the collapse in the Internet economy and other subsequent independent events. Indeed, as the District Court explained, the facts admitted in the PTAC established that

petitioners' At Home shares lost all their value for these other reasons long before AT&T's purported misappropriations could have been known to the market. App. 34a-39a.

Second, the District Court held that petitioners' remaining allegations of an undisclosed AT&T "scheme" to harm At Home did not state a claim for securities fraud. It concluded these allegations represented acts of "corporate mismanagement and abuse" that are actionable only under state law, and not as "securities fraud." App. 29a. Specifically, the District Court held that the scheme alleged here involved, at most, purported "corporate abuse, misconduct and diversion of assets, but no transactions in the relevant securities. Its success depended on the misappropriation of At Home's propriety technology, without regard to any transactions in At Home stock." App. 27a-28a. To the extent petitioners complained that AT&T's conduct had lowered the price at which Cox and Comcast agreed to sell stock to AT&T in March 2000, the District Court held that this was "antecedent, but not integral, to" any scheme affecting purchasers of AT&T's stock. App. 28a. For these reasons, the Court held that AT&T's scheme was not "in connection with the purchase or sale of securities." *Id.*

In addition, the District Court dismissed petitioners' claim that At Home had violated § 14(a) of the Securities Exchange Act when it did not disclose AT&T's alleged "scheme" in the proxy solicitation that sought shareholders' approval of the March 2000 agreements that gave AT&T voting control of At Home. The Second Circuit affirmed the District Court's dismissal of these claims as well

(App. 4a), and petitioners have not sought review of these rulings.

REASONS FOR DENYING THE PETITION

The summary order of the Second Circuit is manifestly unworthy of this Court's review. This case is a contrived attempt to take state law claims for mismanagement of a corporation by a controlling shareholder – which were previously fully litigated and settled for $400 million – and now bring them as a federal securities fraud action. Petitioners made this attempt by alleging misrepresentations and omissions that were barred on the face of the complaint because of the absence of loss causation and by then contending that the existence of these alleged misrepresentations allowed the petitioners to use the securities laws to challenge purported acts of corporate mismanagement that allegedly weakened At Home financially during the class period.

The dismissal of this action was a correct application of well-settled principles to a set of factual allegations that petitioners have conceded are *sui generis*. It does not conflict with any decision of this Court or of any other federal court of appeals. The only way petitioners can even argue otherwise is by misstating the lower courts' holdings.

I. DISMISSAL OF THE "SCHEME" CLAIMS WAS A CORRECT APPLICATION OF SETTLED PRINCIPLES

The primary issue that petitioners seek to have this Court review is the lower courts' holding that petitioners cannot use the federal securities laws to litigate claims that a controlling shareholder breached fiduciary duties to the corporation and to

minority shareholders by engaging in self-dealing and otherwise acting to harm the corporation. However, as this Court and federal courts of appeals have repeatedly held, such allegations raise claims under state corporation law and cannot be converted into federal securities fraud claims by alleging that it was a fraud for the corporation to fail to disclose the breaches of fiduciary duties or the acts of mismanagement by the controlling shareholder. *See Santa Fe Indus., Inc. v. Green,* 430 U.S. 462 (1977). *Santa Fe* concluded that this alleged misconduct is not actionable under the plain meaning of Section 10(b). *Id.* 473-77. The Court further held that even if the terms of Section 10(b) were ambiguous, the Court would not construe them in a manner that would permit state breach of fiduciary duty claims to be brought in federal courts, for that would federalize much of state corporation law and create complex issues of apportioning damages. *Id.* at 477-79.

Petitioner's assertion (Pet. at 18) that Section 10(b) provides a remedy for any undisclosed breaches of fiduciary duties is simply wrong. In addition to *Santa Fe,* this Court has held that Section 10(b) is not an "all-purpose breach of fiduciary duty ban" (*United States v. O'Hagan*, 521 U.S. 642, 655-56 (1997)) and that "internal corporate mismanagement" is outside the Act. *Superintendent of Ins. of State of N.Y. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 9-12 (1971); *accord SEC v. Zandford*, 535 U.S. 813, 820 (2002).

The decision that the lower courts relied upon – *Mutual Shares Corp. v. Genesco, Inc.*, 384 F.2d 540, 545-46 (2d Cir. 1967) – was a precursor of *Santa Fe. Mutual Shares* dismissed securities law claims brought by minority shareholders where, as here, a

majority shareholder had acquired a controlling block of shares from third parties and had not disclosed an alleged scheme to loot the corporation. *Mutual Shares* held that such allegations present only state law claims and that any claim of fraud here is not "in connection with the purchase or sale of any security" within the meaning of the Securities Exchange Act. 15 U.S.C. § 78j(b).

Petitioners here purport to accept the rule of *Santa Fe* and *Mutual Shares*. Pet. at 19. But they argue that the rule should not apply to this case because petitioners alleged (1) that it was a misrepresentation or omission for At Home to represent that it was protecting its intellectual property without disclosing that AT&T was misappropriating it and (2) that AT&T's acts of mismanagement were intended to enable the misappropriations by weakening At Home and were thus somehow part of a single overall nefarious "scheme." But the rule of *Santa Fe* would be meaningless if it could be evaded through such allegations.

Here, moreover, the claimed misrepresentations and omissions were barred on the face of the complaint by petitioners' failure and inability to plead loss causation under *Dura*. If petitioners' scheme theory were accepted, the only issues that would have been litigated in this case would have been whether it had been a breach of AT&T's fiduciary duties for it to have done such things as requiring At Home to increase its capital spending, refusing to provide At Home with favorable financing, deciding to offer open access to other Internet service providers, and obtaining access to At Home's intellectual property for purposes of testing open access or helping At Home address provisioning

problems. PTAC, ¶¶ 59, 60, 81, 83, 89, 91(b) & 100. These allegations epitomize matters that are exclusively addressed under state corporate law and that cannot support a claim of securities fraud.

Against this background, it is ironic that petitioners' principal argument is that the Second Circuit here decided the same question involving the scope of "scheme" liability under SEC Rule 10b-5(a) & (c) that is now before the Court in the *Stoneridge* case and in a second case that presumably is being held for *Stoneridge*.[2] In particular, petitioners contend the Second Circuit has "limit[ed] the scope of conduct prohibited by Rule 10b-5 to misrepresentations," and has "further exclud[ed] deceptive conduct from consideration as part of a scheme to defraud" – in conflict with decisions of the Fifth, Eighth, and Ninth Circuits. Pet. at 29.

But the Second Circuit's summary order did no such thing. It summarily affirmed a decision of the District Court that held that "subparagraphs (a) and (c) of Rule 10b-5 do *not* require a misstatement or omission" and that did not address whether deceptive conduct is actionable. *Id.* at 19a (emphasis added). The Second Circuit simply held that "the plaintiffs here have failed to allege that the AT&T defendants' conversion scheme was in connection with the

---

[2] Pet. at 28-31. *In re Charter Commc'ns, Inc. Sec. Litig.*, 443 F.3d 987 (8th Cir. 2006), *cert. granted sub nom. Stoneridge Inv. Partners, LLC* v. *Scientific-Atlanta, Inc.*, 127 S. Ct. 1873 (2007) (No. 06-43); *Regents of Univ. of Calif. v. Credit Suisse First Boston, Inc.*, 482 F.3d 372 (5th Cir. 2007) ("*Regents*"), *petition for cert. filed*, 75 U.S.L.W. 3557 (U.S. Apr. 5, 2007) (No. 06-1341); *see also Simpson v. AOL Time Warner Inc.*, 452 F.3d 1040 (9th Cir. 2006), *petition for cert. for filed*, 75 U.S.L.W. 3236 (U.S. Oct. 19, 2006) (No. 06-560).

purchase or sale of securities" because it involved claims of mismanagement that are not actionable as securities fraud. App. 3a. As to that holding, there is no conflict among the courts of appeals.

By contrast, *Stoneridge*, *Simpson*, and *Regents* concern "the scope of primary liability for *secondary* actors." *Regents*, 482 F.3d at 386. In all three cases, the issue was whether non-speaking parties could be liable as primary violators of Section 10(b) when they engaged in transactions with a public corporation with no legitimate business or economic purpose except to inflate artificially the public corporation's financial statements. *Stoneridge* Pet. at i (question presented). The Ninth Circuit held that "such conduct may be in connection with the purchase or sale of securities if it is part of a scheme to misrepresent public financial information where the scheme is not complete until the misleading information is disseminated into the securities market." *Simpson*, 452 F.3d at 1052.

This case does not remotely present any such issues. There is no issue here involving the liability of secondary actors who are not alleged to be "control persons" under § 20(a) of the Securities Exchange Act. Nor does the case present the issue whether 10b-5 liability can be based on "deceptive devices" other than misrepresentations or omissions. Similarly, the Second Circuit did not here address a scheme that had the purpose of misleading the markets through inflated financial statements and that was not "complete until misleading information is disseminated." *Simpson*, 452 F.3d at 1052. Rather, it simply held that the alleged scheme to harm At Home – which did not involve any actionable misrepresentations or omissions and whose purpose

was allegedly to steal At Home's proprietary information for AT&T's own use – was not in connection with the purchase or sale of securities. App. 3a. *See also* App. 26a-29a.

In short, the Second Circuit's decision does not even address the issue in *Stoneridge*, *Simpson*, and *Regents*, much less conflict with those cases. There is thus no reason to hold this case for *Stoneridge*.

In addition, petitioners are wrong insofar as they are also asserting that the holding that petitioners' mismanagement claims were not "in connection with the purchase or sale of securities" conflicts with prior decisions of this Court. Pet. at 18. The decisions on which petitioners rely hold that to constitute a deceptive scheme in connection with the purchase or sale of securities, stock transactions must coincide with or be an integral part of the deceptive scheme. *See Zandford*, 535 U.S. at 815-16 (broker sold client's securities, redeemed checks, and embezzled proceeds without disclosure to client where broker had a duty to disclose); *United States v. O'Hagan*, 521 U.S. 642, 655-56 (1997) (fiduciary used confidential information to purchase and sell securities without disclosure to his principal where fiduciary had a duty to disclose); *Superintendent of Ins. of State of N.Y. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 7-9 (1971) (defendants "duped" company's directors into authorizing sale of company's treasury bonds in exchange for company's own assets where they had duty to disclose).[3] As the

---

[3] *See also Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 152-55 (1972) (alleged misrepresentations were used by bank employees for the purpose of acquiring stock below its fair value); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, 547 U.S. 71, 85 (2006) (noting that the fraud must, at least, "'coincide' with a securities transaction" and expressly following

District Court here held, AT&T's alleged scheme was independent of any stock transactions, for it "depended on misappropriation of At Home's proprietary technology, without regard to any transactions in At Home's stock." App. 28a. The Second Circuit summarily affirmed this holding.

In this regard, it is irrelevant that AT&T entered into an agreement that provided for the acquisition of a block of shares from Cox and Comcast that gave AT&T undisputed voting control of At Home during the class period. This Court has held that claims under Section 10(b) cannot be based on otherwise legitimate securities transactions independent of the alleged fraud. *See Zandford*, 535 U.S. at 819-820 (the "in connection with" requirement is not met where "after a lawful transaction had been consummated, a broker decided to steal the proceeds and did so" or where "a thief simply invested the proceeds of a routine conversion in the stock market"). Here, the District Court correctly applied this standard, holding that the transaction with Cox and Comcast was "antecedent to" and independent of the alleged fraud. App. 28a.

This principle has special force here because petitioners do not allege that there was any deception in AT&T's agreement to acquire securities from Cox and Comcast. App. 28a, 29a & 41a. In this regard, even if AT&T's conduct somehow lowered the stock price that it would have to pay Cox and Comcast (*see* Pet. at 10), that conduct is irrelevant to the claims petitioners have brought on behalf of all persons who allegedly *purchased* At Home's shares at artificially inflated prices during the class period. *Id.* at 2.

---

and reaffirming *Zandford* in the context of affirmative misrepresentations to the marketplace).

Petitioners also attempt to justify review of these issues by contending that SEC Regulation S-K, Item 404(a) required AT&T to disclose its misappropriations of At Home's intellectual property in the proxies that were sent to shareholders in connection with the March 2000 agreements and in other SEC filings. Pet. at 21. This claim, too, is unworthy of this Court's review. This SEC Regulation requires disclosures of "transactions" between major shareholders and a corporation. AT&T's alleged misappropriations of At Home's intellectual property is not a "transaction" within the ordinary meaning of this term, and this term, too, cannot be construed in a manner that would make state law breach of fiduciary duty claims actionable as securities fraud. *See Santa Fe,* 430 U.S. at 477-79. Further, the Second Circuit's correct construction of this SEC regulation does not conflict with the decision of any court, and the Petition does not even attempt to identify such a conflict.

Finally, there is no substance to petitioners' claim that the decision below should be reviewed because that will resolve intra-circuit conflicts and provide "certainty and predictability" in the Second Circuit. Pet. at 17. Quite apart from the fact that the summary order is a correct application of settled law, the Second Circuit's Rule 32.1(b) provides that "rulings by summary order do not have precedential effect."

II. THE APPLICATION OF *DURA* PRESENTS NO ISSUE FOR REVIEW

Petitioners also ask the Court to review the lower courts' application of *Dura* and their holding that petitioners' separate misrepresentation and omission claims were barred by their failure to allege loss

causation. Petitioners do not contend that there is a conflict between the Second Circuit's decision and the decisions of any other court of appeals regarding the proper application of *Dura*. Instead, they merely assert that over three thousand cases have cited *Dura*. But the volume of cases citing *Dura* does not demonstrate the existence of an important question that is appropriate for review in this Court. Here, the decision below was a correct application of *Dura* and of the uniform decisions of other federal courts of appeals to the unique facts of this case.

Loss causation is an essential element of any securities law claim under Section 21D(b)(4) of the Securities Exchange Act of 1934. In *Dura*, this Court held that loss causation is not adequately pled when a plaintiff alleges only that the alleged misrepresentation or omission caused it to pay an inflated purchase price. Rather, a plaintiff must also plausibly allege that the subsequent decline in price was caused by revelation of the "truth" and not by changed "economic" or market conditions or "other events." 544 U.S. at 343-44, 347. Courts of appeals have thus uniformly held that to plead loss causation, a plaintiff must allege that the stock price later declined in response to either (1) a corrective disclosure that revealed the falsity of the misrepresentations; or (2) subsequent events that "materialized" the risk that was concealed by the misrepresentation or omission. *See, e.g., Teachers' Ret. Sys. of La. v. Hunter*, 477 F.3d 162, 187-88 & n.3 (4th Cir. 2007); *Ray v. Citigroup Global Mkts., Inc.*, 482 F.3d 991, 995-96 (7th Cir. 2007); *Lentell v. Merrill Lynch & Co., Inc.*, 396 F.3d 161, 175-76 (2d Cir.), *cert. denied*, 546 U.S. 935 (2005); *Robbins v.*

Koger Props., Inc., 116 F.3d 1441, 1447-48 (11th Cir. 1997).

Here, as the District Court held, petitioners' complaint established that the decline in At Home's stock price during the class period was not caused by a corrective disclosure or by the materialization of any risks concealed by the alleged misrepresentations and omissions. The specific alleged misrepresentation here is that At Home's statements that it protected its intellectual property were false because those statements did not disclose that AT&T was misappropriating At Home's intellectual property. But petitioners specifically alleged that AT&T's misappropriations of At Home's intellectual property and AT&T's alleged scheme were "never revealed to the public" during the class period. PTAC, ¶¶ 8, 60. Petitioners' allegations also establish that there was no realization of concealed risks during the class period. For they also alleged that AT&T's copying of At Home's intellectual property "did not diminish the usefulness and general potential of [this] technology" to At Home during the class period (PTAC, ¶ 6) and that AT&T did not actually establish its own network and begin competing with At Home until December 2001, months after At Home had filed for bankruptcy and its stock had lost its value. PTAC, ¶¶ 111-12; PTAC, ¶ 6.

Petitioners' admissions thus established that the stock market learned the "truth" about the alleged misappropriations only after the class period ended and after petitioners' stock had lost all its value due to other changed "economic" or "market" conditions (*i.e.*, the bursting of the Internet stock market bubble). *See Dura*, 544 U.S. at 341-43. In short, the decision below was a correct application of *Dura* (and

of the uniform decisions of other courts of appeals) to the unique facts of this case.

Indeed, the arguments that petitioners now make are all simply challenges to *Dura* itself. They contend that *Dura*'s requirement of loss causation should be eliminated, or relaxed, in cases where intentional conduct is alleged. But intentional conduct was at issue in *Dura*, for *every* case arising under Section 10(b) requires the pleading of an "intent to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193-94 & n.12 (1976).

Finally, petitioners also contend that loss causation should have been found for two alleged "misrepresentations" that purportedly "directly caused the price of At Home stock to decline" – the December 6, 1999 open access announcement and the March 29, 2000 announcement that AT&T was entering into an agreement to acquire stock from Cox and Comcast that would give AT&T voting control of At Home. Pet. at 31. But the lower courts did not address these claims because they correctly held that the alleged misstatements were not in connection with the sale of securities and were independent of the events that were alleged to have caused *purchasers* of At Home stock to pay *inflated* prices. The latter holding is correct for the reasons stated above, and there plainly is no basis for the Court to review a hypothetical loss causation claim that has not been addressed by lower courts.

CONCLUSION

This petition for writ of certiorari should be denied.

Respectfully submitted,

WAYNE WATTS
SENIOR EXECUTIVE VICE PRESIDENT AND GENERAL COUNSEL
AT&T CORP.
175 E. Houston Street
San Antonio, TX 78205
(210) 351-3300

DAVID W. CARPENTER*
STEPHEN C. CARLSON
RACHEL B. NIEWOEHNER
DANIEL S. RYAN
SIDLEY AUSTIN LLP
One South Dearborn Street
Chicago, IL 60603
(312) 853-7000

EDWARD R. BARILLARI
SENIOR VICE PRESIDENT AND ASSISTANT GENERAL COUNSEL
AT&T CORP.
One AT&T Way
Bedminster, NJ 07921
(908) 532-1885

Counsel for AT&T Respondents

JONATHAN E. RICH
PROSKAUER ROSE LLP
2049 Century Park East
Suite 3200
Los Angeles, CA 90067
(310) 284-5644

Counsel for Respondent Mark McEachen

November 13, 2007

* Counsel of Record